BLOCK 2
SALARIES

BLOCK 2 SALARIES

In the previous block, you have learnt about the basic definitions, residential status and exempted incomes. You know income tax is levied on the income of the assessee keeping in view his residential status. This block consists of three units and they cover the several aspects of taxation of salary income.

Unit 5 Salaries-I

This unit discusses the definition and chargeability of Salary Income. It also highlights the various components of salary income like Wages, Bonus, Pension, Annuity, and Encashment of Earned Leave on Retirement. This unit also highlights the provisions relating to Death-cum-retirement Gratuity, Advance Salary, Allowances and Profits in Lieu of Salary

Unit 6 Salaries-II

This unit deals with the concept of Perquisites and its different kinds available to all employee and specified employees and the mode of valuing them for bringing them to charge. This unit also highlights the various tax free Perquisites. It also deals with the permissible Statutory Deductions from salary income.

Unit 7 Salaries-III

This unit deals with the various aspects of Provident Funds Schemes including P.P.F and their tax-treatment .It also deals with Deductions available from Gross Total Income in respect of savings, e.g.- Life insurance premium paid, provident fund contributions and other qualifying expenditure under Section 80C.

UNIT 5 SALARIES-I

Structure

5.0 OBJECTIVES

After studying this Unit, you should be able to:

- define the term salary;
- list the items included under the heads salaries; and
- explain the provisions of Income Tax Act, 1961 in relation to the above items.

5.1 INTRODUCTION

A person has to pay tax on the income earned by him in the previous year on the basis of his residential status. "Income from Salary' is one of the main heads of income. In this unit, you will learn the definition of the term 'salary' and the items included in the salary income. You will also learn the calculation of the items to be included in salary for tax purpose.

5.2 MEANING OF SALARY

Any remuneration paid by an employer to an employee for the services rendered by him is called salary. Salary for income tax purpose not only includes the cash received but also includes the value of facilities and benefits provided to the employee.

The income taxable under the head salaries includes:

1) Any salary due from an employer, or former employer in the previous year, whether paid or not.
2) Any salary paid or allowed to an employee in the previous year by or on behalf of any employer though not due or before it becomes due to him.
3) Any arrear of salary paid or allowed to him in previous year by or on behalf of employer or a former employer, if not charged to tax for any earlier previous year.
4) Any wages paid from current or former employer in previous year.
5) Any pension received by employer in previous year.

Gross Salaries	=	Cash receipts e.g. cash salary or wages. Bonus commission Allowance etc.	+	Perquisites e.g., Monetary value of House, Car, Servant, Gas, Electricity, Water, Education etc.	+	Profits in Lieu Salary

Definition

According to Section 17 (1) of the Income Tax Act, the term 'salary' includes:

a) Basic salary or Wages;
b) Bonus;
c) Commission, fee and interim relief;
d) Over time payments;
e) Annuity;
f) Advance salary and arrears of salary;
g) Annual accretion in employee's recognized provident fund;
h) Taxable part of transferred balance;
i) Contribution made by central government in previous year under notified pension scheme in employees account referred to in section 80CCD;
j) Encashment of earned leave;
k) Gratuity;
l) Pension;
m) Compensation on retrenchment;
n) Amount received on voluntary retirement.

5.2.1 Some Important Points Regarding Salary

There are some points related to salary, which are to be kept in mind. The understanding of these points is very important and it will help you in computing the taxable salary of an individual. They are as follows.

i) Salaries and Wages: The income tax act makes no distinction between the salaries i.e., remuneration received by executive and wages i.e., remunerates received by workers. Salaries and wages both are to be taken under the head salaries.

ii) **Relationship of employee and employer:** Any payment will fall under the head 'salaries' only when there exists a relationship between employer and employee and between the payer and the payee. A person may hold an office and still may not be an employee, for example, a director of a company.

iii) **Salaries and Professional Income**: A profession involves the making of successive employment. If such employment is incidental to the exercise of profession, the remuneration received thereby will be taxed under Section 28. For example, if a Chartered Accountant is appointed to audit the accounts for a particular year, the income from such a contract is professional income and if he is employed to look into the accounts of the company regularly, the income so received will be salaried income.

iv) **Payment made after cessation of employment**: When the employee leaves the organization, the employer pays him certain sum like gratuity etc. Any such payment though received after the employee leaves the organization is taxable under the head salaries as it is received for service rendered in past.

v) **Tax-free salary:** Sometimes, the employer deducts the tax at source and pays net salary to the employee. In such cases, the individual has to show the aggregate salary i.e. net salary plus tax paid in his gross total income.

vi) **Deductions by employer**: There are certain compulsory deductions from salary like contribution to provident fund or charges for providing accommodation which are deducted by the employer and the net salary is given to the employee. Even though the amount has been deducted, it is included in the salary income. The reason is that it is only the application of income.

vii) **Dearness Pay:** It is a part of basic salary and is assumed to be given under the terms of employment, but for the valuation of rent free house, house rent allowance, gratuity (other than gratuity under the Payment of Gratuity Act), leave salary, recognized provident fund, and perquisite of gas, electricity, water, it shall be treated as part of basic salary only when it enters into the computation of superannuating or retirement benefits of the assessee concerned.

viii) **Due date of salary**: The rules are as follows:

a) For government and semi-government employee, the salary is due on first date of next month i.e., salary for February is due on 1st March. For this purpose, previous year salary will be from 1st March to 28th February of next year.

b) For bank employees and non-government organizations, the salary is due on last date of same month i.e., salary for February is due on 28th February. For this purpose, previous year salary will be from 1st April to 31st March of next year.

ix) **Dearness allowance**: If it is paid under the terms of employment – Dearness allowance is deemed to be under the terms of employment in the following two cases:

a) When it is included in 'salary' for the purpose of computation of annual contribution in the recognized provided fund;

b) When it is included in 'salary' for the purpose of computation of retirement benefits payable to an employee.

x) **Voluntary payments**: Every payment, in cash or in kind, made by an employer to his employee in consideration of his service under a contract of service or voluntarily is taxed under the head 'salaries'. Thus, salary, perquisite or allowance may come as a gift to an employee, yet it would be taxable. Any payment made by employer to his employee will not be excluded from his salary income merely because the employer made it voluntarily.

xi) **Salary foregoing or surrendering**: Section 15 of the Income Tax Act, 1961, charges salary on due basis. Tax liability is created at the time the salary becomes due. If an employee foregoes or surrenders his salary, he cannot escape from his taxliability.

xii) **Deduction from salary**: Deductions made by the employee out of the salary due to an employee are regarded as application of income. These deductions may be compulsory or optional or under a contract or voluntarily. In every case, deductions from salary are regarded as applications ofincome.

xiii) **Place of accrual of salary**: According to Section 9 of the Act, salary is deemed to accrue at the place where the service for which it is paid, is rendered. Salary accrued in India is deemed to accrue or arise in India though it has been paid outside India.

5.2.2 Definition of Salary for Different Purposes

The definition of 'salary' differs for different purpose. The purpose for which the definition of salary would differ is as follows:

i) Computation of taxable income under the head salaries.

ii) Calculating the exempted amount of House rent allowance under Section 10(13A).

iii) Calculating the value of rent-free accommodation or accommodation provided at a concessional rate.

iv) Calculating qualifying amount of provident fund contributions.

v) Calculating the entertainment allowance.

vi) Calculating exempted gratuity, exempted portion of encashment of earned leave etc.

vii) Calculating perquisite value of gas, electricity or water.

viii) Determination of salary of Rs. 50,000 regarding taxability of perquisites under Section 17(2) (iii)(c) (specified employees).

ix) Compensation on retrenchment under Section 10(10B)

Chart 5.1 will help you to know the meaning of 'salary' for different purpose at a glance.

Chart 5.1: Different Meanings of 'Salary' for Different Purposes

For computation of taxable income under the head salaries	*Rent-free House or Concession in rent*	*House Rent Allowance*	*Qualifying Amount of Contribution to R.P.F.*	*Entertainment Allowance*	*Standard Deduction u/s 16(1)*	*Gratuity*	*Determination of salary or Rs. 50,000 regarding taxability of per quisites under Sec. 17(2) (iii)(c)*	*Compensation u/s 10(10B)*	*Voluntary retirement Sec 10(10C)*
1. Basic Salary or wages. 2. Advance Salary. 3. Arrear of Salary. 4. Annuity or Pension. 5. Gratuity. 6. Fees, Commission Bonus. 7. Allowances including Dearness. Allowances 8. Profits in lieu of Salary 9. Perquisites 10. Excess Contributionto R.P.F. by employer over 12% of salary 11. Excess interest received fromR.P.F. over 9.5% rate of interest will be taxable. 12. Taxable portion of transferred balanceto R.P.F.	1. Basic Salary (excluding advance or arrears of salary received) 2. Taxable Allowance. 3. Bonus. 4. Commission 5. Any other payment in cash (Excluding dearness allowance not entering into retirement benefits of the employee, employer's contribution to R.P.F., Allowances exempt from tax, deductible amount of entertainment allowances, and value of Perquisites.)	1. BasicSalary. 2. Dearness Allowance if the terms of employment to provide, i.e., it is taken into account for retirement benefits, or dearness Pay. (Excluding all other allowances, bonus or perquisites and allextras). 3. Commission based on fixed percentage of turnover achieved by the employee and given under terms of employment.	Same as for House Rent Allowance as per proceeding column.	Basic Salary exclusive of any allowance, benefit or other perquisite.	Total of taxable salary i.e., Gross taxable salary	Basic salary plus DA as per under the terms of employment, commission based on fixed percentage of turnover.If the employee is covered by the Gratuity Act., D.A shallalways be included in salary.	1. Basic Salary, 2. Dearness allowance, 3. All other allowances, 4. Bonus, Commission, etc. and all monetary payments included in gross salary after allowing deduction u/s 16. For this purpose, salary will not include perquisites as they are not received in cash.	1. Salary, 2. allowances, 3. value of rent-free or concessional accommodation, 4. Light, water orany other amenity and travel concession; but does not include Bonus, Gratuity, and employer's contribution to any fund for retirement benefits.	1. Basic salary last drawn + D.A. (if under the terms of employment) + Commission on sales (basic on fixed% of sales)

Testimonials and personal gifts

Testimonials and personal gifts which are given purely out of personal affection and regard, although received by an employee from his employer would not be chargeable to tax as salary income. But, during the previous year, the value of such gift, voucher or token is upto Rs. 5,000 in the aggregate the value of perquisite shall be taken as NIL. But, if the aggregate value of gifts per annum is above Rs. 5,000, the excess amount of gift will be a taxable perquisite.

5.3 MAIN ITEMS INCLUDED IN SALARY

5.3.1 Salary or Wages

Let us analysis the components of salary income one by one.

In the eyes of law and as per the principle, there is no difference between salary and wages receivable by a laborer and the salary receivable by the corporates, are taxable under head 'Salaries'. From income tax point of view there is no difference between the two terms. Both salary and wages are taxed under the head salaries.

The study of computing process of taxable salary may be studied in the following headings:

a) Computation of gross salary
b) Deductions out of gross salary
c) Computation of taxable salary

Gross Salary

(I) Salary
[Salary due, or salary received or arrears of salary]
Salary includes:
i) Wages
ii) Annuity or pension
iii) Gratuity
iv) Fees, commission, perquisites or profits in lieu of or in addition to salary
v) Advance salary
vi) Encashment of leaves
vii) Annual accreation to recognised provided fund
viii) Transferred balance
ix) Voluntary payments
x) Contribution by the Central Government or any other employer to employees pension scheme U/S 80CCD during the previous year.

(II) Allowances
i) Fully taxable
ii) Partly taxable
iii) Fully exempt

(III) Perquisite
i) General perquisites
ii) Specific perquisites
iii) Tax free perquisites

IV) Profits in Lieu of salary
i) Compensation for the loss of or the variation in the terms of service
ii) Any payment by the employer to his employee in appreciation of his services
iii) Amount received from provident or other fund

Fig. 5.1: Gross Salaries

Salary or Wages

The terms 'salary' may be taken to denote payments made to a white collar worker or higher category of employees like assistants, officers etc. while 'wages' may denotepayments made to blue collar worker or casual labourers etc. The distinction is not material for Income tax purpose as both the payments are chargeable under the head 'salaries'.

Under Section 17(1) of Income Tax Act, the term 'salary' includes the following receipts:

a) Basic salary or Wages;

b) Bonus;

c) Commission, fee and interim relief;

d) Over time payments;

e) Annuity;

f) Advance salary and arrears of salary;

g) Annual accretion in employee's recognized provident fund;

h) Taxable part of transferred balance;

i) Contribution made by central government in previous year under notified pension scheme in employees account referred to in section 80CCD;

j) Encashment of earned leave;

k) Gratuity;

l) Pension;

m) Compensation on retrenchment;

n) Amount received on voluntary retirement.

Illustration 1

Shri Shanker Dayal has been getting a salary @ 3,600 per month since 1st April 2020. He has been allowed an increment of Rs. 200 on 1st August, 2020. Compute his basic salary.

Solution:

Computation of basic salary of Shri Shanker Dayal for the Assessment Year 2021-22

	Rs
April 2020 to July 2020 (Rs.3,600×4)	14,400
August 2020 to March 2021 (Rs.3,800×8)	30,400
Basic Salary	**44,800**

5.3.2 Encashment of Earned Leave on Retirement

An employee may be allowed to avail different types of leave e.g. medical leave, casual leave and earned leave. Some employers give cash for these leaves. Encashment of earned leave is also known as 'leave salary'. It is an incentive to an employee not to enjoy leave standing to his credit. If he does not avail of the leave which he is entitled to avail, he is paid equivalent cash salary for the leave not availed by him. This payment is termed as 'encashment of earned leave'. If the earned leaves are encashed during service, whole amount of cash received shall be taxable to all types of employees, whether government or non-government employees. The employee can demand for relief under Section 89(1).

Encashment of leave at the time of retirement/death: When an employee takes retirement from the service or resigns from service, he is given some amount for his earned leave. It is called encashment of earned leave or leave salary. It is also called discounting of leaves. Some part of this money received by the employee is taxable and remaining part shall be exempted. The provisions of Income Tax Act regarding exemption of encashment of earned leave are given below:

1) **Government Employee:** The whole amount of sum received by the employee of Central and State Government as encashment of earned leave at the time of his retirement (whether on superannuation or otherwise) or on resignation is fully exempt from tax. This exemption is also available on voluntary retirement but does not include termination of service. Thus, this exemption is not available on termination of service. Encashment received by the family members of government employees is also exempt from tax.

   'Leave salary' paid to the legal heirs of deceased employee in respect of privilege leave standing to his credit at the time of his death is not taxable as salary. It is fully exempt.

2) **Non-Government Employee (including employees of Local Authority, Statutory Corporation and Public Sector Enterprises):** Least amount of following four items shall be tax free. Remaining amount shall be included in salary.

   a) Actual amount of encashment of earned leave received or;

   b) Salary of maximum 10 months calculated on the basis of average salary of 10 months preceding immediately from the retirement.

   c) Calculated amount of encashment of leave for the approved period not taken during the services. (Maximum period of 30 days for each completed year is approved for encashment of earned leave),or

   d) The amount specified by the government, i.e. Rs. 3,00,000

Note:

i) Meaning of salary= (Basic Salary + Dearness Pay + Dearness Allowance (if under terms of employment)+ Commission at fixed rate on turnover by employee).

ii) While calculating the earned leave, the total number of years of service completed will be taken only but the incomplete number of months or days will be ignored.

Illustration 2

Mr. X is the general manager of Plus Ltd. He draws a salary of Rs. 5,500/- per month. He retires on 31st December 2020, after completing 26 years and 11 months of service. He is entitled to one month earned leave for every year of completed service. Rs. 1,00,000 received for encashment of earned leave on retirement. He has availed of 20 months earned leave while in service. He has encashed the unutilized earned leave standing to his credit on the basis of last drawn salary. Compute the taxable amount of leave encashment of Mr. X for the assessment year 2021-22.

Solution:

Computation of Taxable Amount of Encashment of earned leave of Mr X for Assessment Year 2021-22

a)	Leave (one month's leave for each completed year of service)	26 months
b)	Leave availed	20 months
c)	Leave due (26 months – 20 months)	6 months
d)	Exempted amount would be least of the following:	Rs.
	1) Actual amount of encashment received	1,00,000
	2) 10 months average salary (Rs. 5,500 × 10)	55,000
	3) Cash equivalent to 6 months @ average salary (5,500 × 6)	33,000
	4) Maximum exemption limit	3,00,000

Taxable amount of Earned Leave = Actual amount received – least of the (1) (2) (3) (4) above i.e. amount of Rs. 1, 00,000 – 33,000 = Rs. 67,000

Hence, Rs 67,000 is taxable amount of Earned Leave.

Gross Salary = Basic salary + Taxable part of leave encashment

= [Rs. 5,500x9 (April, 2020-Dec, 2020)] + Rs. 67,000

= Rs. 49,500 + Rs. 67,000 = Rs. 1, 16,500

Illustration 3

Shri Omkar Narain was employed in a company. He took voluntary retirement on 1st December, 2020 after completing 25 years of service. On 1st January, 2020 his salary was Rs. 8,000 p.m. after adding the annual increment. In this company, two months leave accrued every year. Compute the amount exempt regarding encashment of earned leave from the following particulars.

	A	**B**	**C**
Total leave availed during service	10 months	Nil	30 months
Actually received amount	Rs. 2,40,000	Rs. 3,00,000	Rs. 1,20,000

Solution:

Average salary Rs. 8,000 p.m

Approved period of earned leave 25 months

(On the basis of 30 days per year).

The least of the following amount will be exempt.

		A	B	C
i)	Salary for10 months on the basis of average salary	Rs. 80,000	Rs, 80,000	Rs. 80,000
ii)	Salary for the period Remaining after deduction leave availed from the approved period	15×8,000	25×8,000	Nil
		1,20,000	2,00,000	Nil
iii)	Maximum limit	3,00,000	3,00,000	3,00,000
iv)	Actual amount received	**A**	**B**	**C**
		Rs. 2,40,000	Rs. 3,00,000	Rs. 1,20,000
	The exempt amount will be	80,000	80,000	Nil

Illustration 4

Determine the exempt amount of the encashment of earned leave from the following particulars.Employees retiring from a limited company on 31st Dec., 2020

Monthly salary at the time of retirement	**A** Rs. 25,000	**B** Rs. 25,000	**C** Rs. 25,000
Duration of service	30 years	30 years	30 years
Leave availed during service	-	20 months	32 months
Leave entitlement is at the rate Of 1.5 month for each year			
Leave at the credit	45 months	25 months	13 months
Leave salary paid to employee	Rs. 6,75,000	Rs. 3,75,000	Rs. 1,95,000

Solution:		**A**	**B**	**C**
i)	Actual amount received	Rs. 6,75,000	Rs. 3,75,000	Rs. 1,95,000
ii)	10 months' salary			
	10 × 25,000	Rs. 2,50,000	Rs. 2,50,000	Rs. 2,50,000
iii)	Encashment of leave	(30 years- 0 months)	(30 years- 20 months)	(30 years- 32 months)
	in credit on the basis of	30×25,000	10×25,000	Nil
	one month for each year of service	7,50,000	2,50,000	Nil
iv)	Maximum amount	3,00,000	3,00,000	3,00,000
	Least of the above four amount will be tax free exemptamount	2,50,000	2,50,000	Nil

Illustration 5

R, an employee of ADB ltd. Retired from the company on 30/11/2020.At the time of his retirement, he receives Rs 2, 88,000 as leave salary from his employer. The following information is provided by the employee:

Salary at the time of retirement (p.m.)	Rs 18,000
Period of service	20 years and 8 months
Leave encashment	Rs 2,88,000
Leave availed while in service	14 months
Balance unavailed leave at the time of retirement	16 months
Average salary for the months of Feb, 2020 to Nov, 2020	Rs 17,600
Leave entitled	1 ½ month for every completed year of service

Compute the amount of taxable leave encashment of R for Assessment Year 2021-22

Solution:

The minimum of the following four amounts will be exempt:

	Rs
1) Leave encashment actually received	2,88,000
2) 10 months average salary i.e. Rs 17,600 ×10	1,76,000
3) Leave encashment for 6 months @ Rs 17,600 p.m.	1,05,600
4) Amount specified by the government	3,00,000

Hence, Rs 1,05,600 would be exempt and the balance of Rs 1,82,400 would form part of gross salary.

Note:

Although R is entitled to 1 ½ months leave for every completed year of service, for the purpose of calculating limit for clause 3 above, the calculations will be done on the basis of maximum 30 days, leave for every completed year of service. Therefore, the maximum leave allowable for purpose of clause 3 i.e. 30 days × 20 = 600 days i.e. 20 months.

Leave already availed by employee is 14 months. Therefore, the unavailed leave calculated on basis of 30 days leave for every completed year of service is 6 months (20-14)

5.3.3 Bonus, Fees, Commission, Profit in Lieu of Salary

An employee may get bonus, Fees, Commission, profit in lieu of salary, interim relief etc. from his employer. Bonus may be monthly, annually or may depend on a certain percentage on sale or any other measurement. This is taxable in the year of receipt. If the employee receives arrears of earlier year's bonus, bonus in a subsequent year, he is entitled to claim relief under section 89(1).

5.3.4 Pension

A person is entitled for pension every month after retirement as per terms of employment. Pension received both by government and non-government employee is taxable under the head 'Salaries'. It is chargeable to tax on accrual basis, whether it is received voluntarily or under a contract. It is periodical or lump sum payment received by an employee from his employer after his retirement from service. It is taxable as salary. But if the employee was receiving tax free salary, the pension payable to his widow would also be tax free, but treated as family pension in income from other sources. A similar rule is applicable to the pension paid by a foreign government to its employees serving in India. But the pension earned and received in the hands of an ordinary resident is taxable. Salary and pension received from UNO is not

Chargeable to tax in India. A new pension scheme has been introduced in the case of an employee joining central government service on or after January 1, 2004. This scheme is mandatory to every employee. The law relating to pension is briefly stated below.

i) Periodical Pension (Uncommuted Pension): Such as monthly, yearly or otherwise paid pension, is chargeable to tax as salary in the hands of all employees i.e. Government as well as non-Government employee.

ii) Commuted Pension: Sometimes, the employee wants to take lump sum payment in lieu of pension on monthly basis. Such lump sum is known as commuted pension. The provisions of such commutation are as follows.

$$\text{Total pension} = \frac{\text{Commuted value ofpension}}{\text{Commuted part of pension}}$$

iii) Commutation of pension Section 10 (10A): Where an employee gets a lump sum as a consideration for commutation of his pension, the sum received constitutes salary in his hands and is taxable according to the followingprovisions:

a) **Commuted pension received by Government employees**

Any commuted pension received by a Government employee shall be fully exempt, also the entire commuted value of pension received by a government servant, who voluntary resigns and join the services of a public sector corporation is exempt.

b) **Commuted pension received by Non-government employees** Commuted pension in this case is exempt from tax, to the extent stated below:

i) Where the employee is in receipt of gratuity, the commuted value of $1/3^{rd}$ of the total pension shall be exempt.

ii) In any other case, the commuted value of ½ of total pension shall be exempt.

Any excess over such exempted amount is taxable as salary, where on account of taxation of commuted pension, the pensioner pays tax on a higher slab rate; he is entitled to relief under section 89(1). Arrears of pension are taxable on due basis, whether received or not.

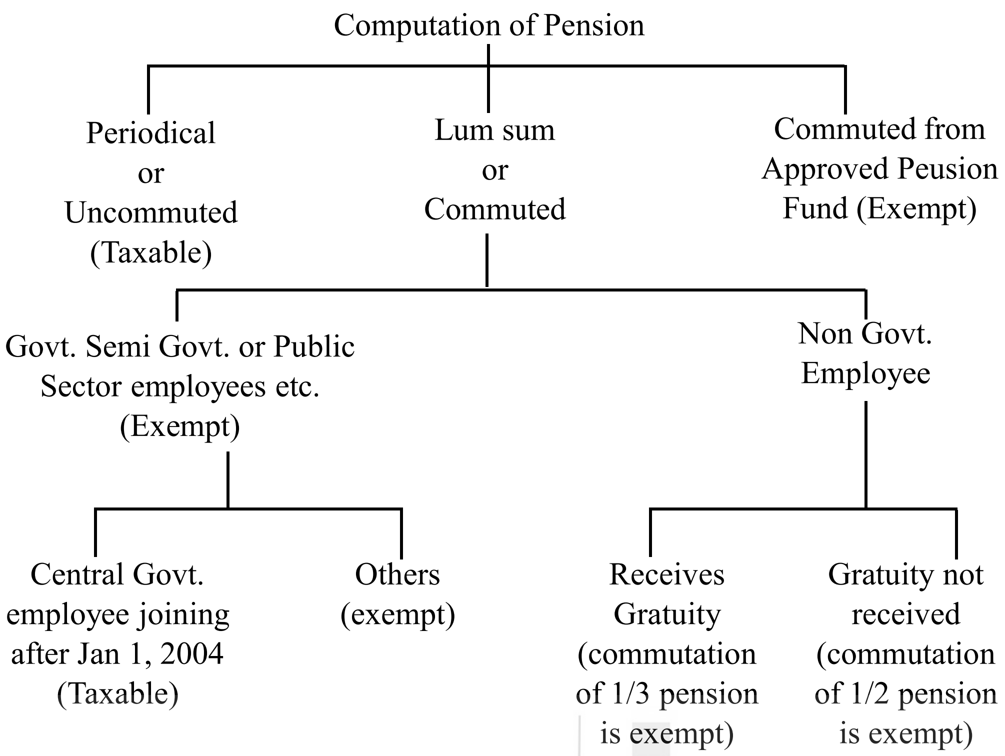

Fig. 5.2: Computation of types of pension

Illustration 6

Mr. Madhur is getting a pension Rs. 4,000 per month from a company. During the previous year he got two-third pension commuted and received Rs. 1,86,000. Compute the exempted amount, if (a) he also received gratuity (b) he did not received gratuity, for the assessment year 2021-22.

Solution:

Mr. Madhur is a non-Govt. employee, Tax Free commuted pension in his case is as below:

a) He received gratuity.	Rs.
Commuted value of 2/3 pension	1,86,000
Commuted value of full pension = 1,86,000 $\times \frac{3}{2}$	2,79,000
Commuted value of $\frac{1}{3}$ pension = 2, 79,000 $\times \frac{1}{3}$	93,000
Hence, Exempt amount will be Rs. 93,000 and balance amount Rs. 1, 86,000 – 93,000) = Rs. 93,000 is taxable.	
b) When Mr. Madhur does not receive gratuity commuted value of 2/3 pension = Rs. 86,000	
Commuted value of full pension = 1, 86,000 $\times \frac{3}{2}$	2, 79,000
Commuted value of $\frac{1}{2}$ pension = 2, 79,000 $\times \frac{1}{2}$	1, 39,500
Hence exempt amount will be Rs. 1, 39,500 and balance amount (1, 86,000 – 1, 39,500) = Rs. 46,500 is taxable.	

Illustration 7

Determine taxable pension for the assessment year 2021-22 in the following circumstance:-

i) Mr. Shantanu retired from ABC Ltd. on June 30, 2020. He got a pension @ Rs. 1,500 p.m. up to November 30, 2020. He got Rs. 1,50,000 on December 1, 2020 as commuted value of his 60% pension. What would have been the position if he also received a gratuity at the time of retirement.

ii) Mr. Harshit retired from the Central Government services on July 1, 2021. He received pension @ Rs. 2000 p.m. up to February, 2021. He got a lump sum of Rs. 1, 00,000 on March 1, 2021 as commuted value of ¼ pension.

iii) Received by an individual during the previous year Rs. 50,000 as commutation of pension from LIC pension fund set up under an approved pension scheme.

iv) Mr. Satish received Rs. 1,800 p.m. as pension from Honda Ltd., a public limited company in private sector, during the previous year.

Solution:

i) Mr. Shantanu is a non-government employee. Uncommuted pension received by him is chargeable to tax. Commuted pension receivable by him is partly tax-free and partly chargeable to tax. Pension will calculate in two parts.

a)	**Uncommuted pension** chargeable to tax is computed Rs. 7,500 as under: Pension @ Rs. 1,500 p.m. from July 1,2020 to November 30, 2020 i.e. for 5 months	
	Pension @ 600 p.m. [Rs. 1,500-60% of 1,500 (Commuted)] from December 1, 2020 to March 31, 2021 i.e. for 4 months	Rs.
	[1500-900] 600 × 4	2,400
	Total Uncommuted pension chargeable to tax	9,900
b)	**Commuted pension chargeable to tax is computed as under:**	
	Commuted value of 60% of the pension	1,50,000
	Commuted value of full pension $\left[1{,}50{,}000 \times \frac{100}{60}\right]$	2,50,000
	i) When Mr. Shantanu does not receive gratuity ½ of the commuted value of full pension is exempt from tax $\left[\frac{2{,}50{,}000}{2}\right]$	1,25,000
	Amount chargeable to tax (1,50,000 – 1,25,000)	25,000
	ii) When Mr. Shantanu receives gratuity 1/3 of the full commuted pension is exempt $\left[\frac{2{,}50{,}000}{3}\right]$	83,333
	Amount chargeable to tax (1,50,000– 83,333)	66,667

Thus, when Mr. Shantanu gets gratuity also then, taxable amount will be Rs. 76,567 (Rs.66, 667 commuted + Rs. 9,900Uncommuted).

When Mr. Shantanu does not received gratuity, then taxable amount will be Rs. 34,900 (Rs. 25,000 commuted + Rs. 9,900 Uncommuted)

ii) Mr. Harshit is an employee of the central government. Commuted pension received by a government employee is wholly exempt under section 10(10-A). Thus, commuted pension of Rs. 1,00,000 is wholly exempt.

Uncommuted pension will be taxable as under:	Rs.
Pension for 8 months @Rs.2,000	16,000
(1, July 2020 to February, 2021)	
Pension for March 2020 after deducting	
The commuted pension i.e. Rs. 2,000 – ¼th of it	1,500
Taxable amount of pension	17,500

iii) Commutation of pension received from LIC pension fund is exempt from tax. Hence, Rs. 50,000 isexempt.

iv) Mr. Satish is a non-government employee and periodical pension i.e. Rs. 1,800 × 12 – Rs. 21,600 is taxable.

5.3.5 Annuity

A certain sum paid for a certain period by the employer to his employee in consideration of service rendered by him is called annuity. It is explained by points given below:

a) Annuity payable by the present employer is taxable assalary.

b) Annuity received from a past employer is also chargeable totax.

c) Annuity from any other person such as from LIC etc, under an insurance policy is taxable as 'income from other sources'.

5.3.6 Gratuity [Section 10(10)]

Gratuity is a gratuitous payment made by the employer to his employee. It is a gift or present, in return for favor of services rendered, at the time of retirement or death. It is paid in recognition of long and meritorious services, rendered by the employee. The payment of gratuity act, 1972 has legally recognized the concept. Even where the act is not applicable, invariably all employers provide for payment of gratuity to their employees through the terms of employment. The amount of gratuity is paid to the employee, if he survives at the time of retirement, or to his wife or children, if he dies before retirement.

The provisions regarding gratuity are stated below:

a) In the case of government employees [Sec10(10)(i)]

Any death – cum – retirement gratuity received by central, state, local government employees is fully exempt from income tax.

b) **In the case of employees covered by the Payment of Gratuity Act, 1972 [Sec 10(10)(ii)]**

Any gratuity received by an employee covered by the Payment of Gratuity Act, 1972 is exempt from tax to the extent as stated below:

i) 15 days salary (7 days in case of employees of a seasonal concern) for each years' service (service for a period of more than 6 months is regarded as one year's service) based on salary last drawn i.e., 15 days salary x length of service, or.

ii) 20,00,000 as maximum amount; or

iii) Actual amount of gratuity received, whichever is less

Taxable gratuity = Actual gratuity received – Exempted gratuity

(Meaning of salary for purpose of computation of gratuity = Last drawn salary + D.A. last drawn by the employee but excluding all other payments)

Note:

1) Any bonus, commission, H.R.A., overtime wages or any other allowances is not included.

2) Salary of 15 days is calculated as below.

$$\text{15 day's salary} = \frac{\text{Salary drawn in last month}}{26} \times 15$$

3) Salary of 15 days in case of piece rated employee is calculated as below:

$$\text{15 days salary} = \frac{\text{Monthly average wages (Including overtime wages) received during last 3 months}}{26} \times 15$$

4) For the purpose of this act, one month is regarded as 26 days.

5) 6 months or more than 6 months shall be considered as one year.

Table 5.2: Gratuity Rules in Brief:

Government (Central, State or Local) Employees of all categories U/S 10 (10) (i)	**Employees covered by the payment of Gratuity Act, 1972 U/S 10(10)(ii)**	**Employees i.e. covered U/S 10(10)(iii) , but, not covered under Payment of Gratuity act, 1972**
Gratuity received is totally exempt	Least of the following amount is exempt: i) 15 days or 7 days salary on the basis of salary last drawn for services of 6 months or more in each year; or ii) Rs. 20,00,000; or iii) Actual Gratuity received **Note:** a) Salary = Salary (including D.A) last drawn by the employee excluding all other payments b) 15 day's salary = $\frac{\text{Salary of last month drawn} \times 15}{26}$	Least of the following amount is exempt: i) ½ months average salary for each completed year of service; or ii) Rs. 20,00,000; or(iii) Actual Gratuity received **Note:** a) Salary = Basic salary +D.A. (if it is under the terms of employment)+Commission on sale (if it is fixed percentage on sales effected by employee). The salary will be average salary, computed on the basis of average salary of 10 months immediately preceding the months of retirement. b) Completed year = Period of full year of service. Any fraction of the year is ignored.

Illustration 8

Mr. Shakil is an employee of Axis Ltd. He receives Rs.5, 00,000 as gratuity as per the provisions of payment of gratuity act, 1972. He retired on 31st March, 2021 after doing service for 27 years and 9 months. At the time of retirement his monthly salary was Rs. 17,000. Calculate the taxable gratuity in the hands of Mr Shakil for Assessment year 2021-22.

Solution:

i) 15 days salary for each completed year of service.	Rs.
Completed year is 28 because fraction of month is more than 6 months.	
$17{,}000 \times \frac{15}{26}$	
9,808 × 28	2, 74,624
ii) Maximum amount	20,00,000
iii) Actual amount received	5,00,000

The minimum amount of above three amount is 2, 74,624 which is exempted and remaining part (5, 00,000 – 2, 74,624) = Rs, 2, 25,376 is taxable as gratuity.

Illustration 9

Mr. Ashutosh was retired from an Indian company after serving 34 years 4 months on 31st December, 2020. The company paid him Rs. 8, 00,000 as gratuity under the payment of Gratuity act, 1972. His monthly salary and D.A. at the time of retirement was Rs. 58,000 and Rs. 5,800 respectively. Compute the exempted gratuity U/S 10(10)(ii) of income tax act.

Solution:

i) 15 days salary for each completed year of service.	Rs.
Salary = 58,000 + 5,800 = $63{,}800 \times \frac{15}{26}$	
= 36,808 x 34	12, 51,472
ii) Maximum amount	20,00,000
iii) Actual amount received	8, 00,000.

Minimum amount of above three is Rs. 8, 00,000 so total amount which is receiving that is exempt from tax.

iii) **In the case of any other employees [Sec 10(10) (iii)] :** The employees who are not covered under the Payment of Gratuity Act, 1972, received gratuity by him or by his widow or by his children on his retirement, death, termination of service, resignation or on his becoming incapacitated prior to his retirement, is exempt from tax to the extent as stated below:

a) ½ month's average salary for each year of completed service; or

b) maximum amount i.e. Rs.20,00,000; or

c) Actual gratuity received.

Note:

1) Meaning of salary for computation of gratuity: Basic salary + Dearness Allowance. + Dearness Pay (if under the terms of employment) + commission (if it is payable at a fixed percentage of turnover.)

2) Average monthly salary is to be calculated on the basis of 10 months' salary immediately preceding the month in which the employee retires.

3) For calculating completed years of service any fractional portion (even if it amounts to 11 months and 29 days) is to be ignored.

4) Any gratuity received in excess of the exempted limit is taxable as salary. However, any gratuity received in excess of the exempted limit is taxable as salary.

5) Where gratuity is received by an employee from more than one employer, either in the same year or in different years. The total amount of gratuity exempt cannot exceed Rs.20,00,000.

Since gratuity is taxed as salary, existence of relationship of employer and employee is vital. For example, the gratuity paid by LIC to its agents does not qualify for any exemption.

Illustration 10

After serving for 33 years and 9 months in Reliance Petro chemicals Ltd. Mr A, who is covered by payment of gratuity act, retires from service on 30th April, 2020. The Company pays him a gratuity of Rs 85,000.His monthly basic salary at the time of retirement was Rs 4,500.

You are required to determine the amount of exempted gratuity under section 10(10) of the income tax act.

Solution:

Mr A is covered under payment of gratuity act, 1972; his total period of service is 33 years and 9 months, hence, 34 years of service will be taken. For computing salary of 15 days, salary of last month will be taken and 15/26 of this salary will be done.

15 days salary = 4,500 × 15/26 = Rs 2,596

The amount of exempted gratuity will be least of the following:	Rs.
a) Actual amount	85,000
b) Rs 2,596 × 34	88,264
c) Maximum	20, 00,000

Exempted gratuity will be Rs 85,000

Illustration 11

Mr Vishesh, who is not covered by the payment of gratuity act, 1972, receives a gratuity of Rs 5, 76,000, when he retires on 23rd June, 2020 after a service of 34 years 9 months and 23 days. His last drawn emoluments are as follows:

Basic salary Rs 30,000, Dearness allowance Rs 7,200 p.m. (Fixed)

Annual increment in basic salary Rs 1,200 p.m. falls due on 1st Jan, every year

What amount of gratuity is exempt from tax in the assessment year 2021-22?

Solution:

Average basic salary for 10 months immediately preceding the month in which he retires Rs 30,000, which has been calculated as under:	Rs.
Salary for 5 months @ Rs 28,800 p.m. (August 2019 to December 2019)	1, 44,000
Salary for 5 months @ Rs 30,000 p.m. (January 2020 to May 2020)	1,50,000
Total salary for 10 months	2, 94,000
Average salary of last 10 months (Rs. 2, 94,000/10)	29,400
Half month's average salary (Rs 29,400/ 2)	14,700

The amount of gratuity exempt u/s 10(10) will be least of the following:

1)	Actual amount of gratuity received	5,76,000
2)	Half month's salary for each year of completed service Rs 14,700 × 34	4, 99,800
3)	Maximum Limit Exempted amount of gratuity 4,99,800 Taxable Gratuity = Rs 5, 76,000 –Rs 4, 99,800 =Rs 76,200	20,00,000

5.3.7 Compensation on Retrenchment

An employee may be retrenched from service under Industrial Disputes Act, 1947.Two points are important in this connection:

i) Retrenchment on winding-up of business;

ii) Transfer of employee from one service to another

If an employee gets some amount of compensation from his employer due to retrenchment, it is included in gross salary. But whole amount of compensation is not taxable. Some part of it is tax-free. Least of the following amounts shall be exempt and remaining taxable amount will be included in the gross salary:

a) Actual amount of compensation received;

b) Salary for service period calculated on the basis of 15 days salary for each completed calendar year (6 months or more shall be treated one year);

c) Amount declared by Central Government Rs. 5, 00,000.

d) 26 days shall be taken for one month

e) Computation of 15 days salary shall be computed as below:

Meaning of average salary
Meaning of salary = Basic salary + Dearness Allowance (Whether it is under terms of conditions or not) + Dearness Pay

Average salary of three months (Including dearness allowance) × $\frac{15}{26}$

Note:

1) A workman means that workman who is covered under Industrial dispute Act. It does not include manager, administer, whose salary is more than Rs 10,000 pm and who render their services for managerial affairs, personnel employed in army, police services and navy services.

2) The workman can demand for relief u/s 89(1), if amount of compensation on retrenchment exceeds above mentioned exempted limit.

5.3.8 Voluntary Retirement [Section 10(10C)]

If any employee of Public Sector Company or any other company or any authority established under any act or any corporation or cooperative society or university or Indian institute of technology established under any central or provincial act or any management institute notified by central government, takes retirement from his service voluntary, whole amount received or receivable in this connection shall be exempt upto a maximum limit of Rs. 5, 00,000.An exemption of maximum Rs. 5, 00,000 shall be allowed. The advantage of such exemption upto Rs 5, 00,000 shall also be given to employees of such concerns which are very famous for all over India or state and these concerns are notified by central government. If any assessee gets sum under such scheme in installments, he will also be entitled to avail this exemption upto a total limit of Rs. 5, 00,000.

Least of the following will be exempt from tax:

i) Actual compensation amount received

ii) Salary of 3 months service period of full year service length

iii) Remaining month of service * salary at the time of retirement

iv) Maximum amount Rs 5, 00,000

Note: [Meaning of Salary- Basic salary + Dearness Pay +Dearness allowance (if it is under terms of employment) + Commission at fixed percentage on sale (if any)]

5.3.9 Advance Salary

Advance salary means the salary received by an employee before it is earned by him it is included in the taxable income of the recipient. But, it is not so included when it becomes due.Tax is chargeable on all salaries

a) Which are due whether actually paid or not and also those

b) Which are paid whether due or not to the employee during the financial year.

In view of this specific provision even advance salary received i.e salary received for services yet to be rendered would also be taxable in the year of receipt although such salary is not yet due to the employee. Thus, salary is taxable at the earliest point of time i.e on the date of accrual or on becoming due or on receipt of salaries.

Advance against salaries

This is loan availed by an employee which will be repaid by him to his employer in installments along with interest or free of interest as the case may be. This loan is not to be treated as salary.

Relief: It is to be noted that when advance salary is taxed in the year of receipt, more than12 months' salary may be taxed in one previous year. This will increase the income limit and higher slab rates may be applied in calculating tax payable, in this type of case, the employee can apply to the assessing officer in the prescribed form for relief which will be granted to him by virtue of the provisions of Sec. 89.

5.3.10 Allowances

All monetary payments made by an employer to his employees, other than salary, are termed as allowance. It is fixed, predetermined and given regularly in addition to salary in connection with the services rendered by the employee. It may be given in form of reimbursement of some expenditure incurred by the employee or may be given irrespective of actual expenditure. From the income tax view point, all the allowances may be classified in three parts, i.e.fully taxable, partially exempted and fully exempted,which are shown in Table 5.2 below:

Table 5.3: Allowances

Fully taxable	Partially exempted	Fully exempted
1) Dearness Allowance or Dearness Pay 2) Medical Allowance 3) Tiffin Allowance 4) Servant Allowance 5) Non-Practicing Allowance 6) Warden Allowance 7) Deputation Allowance 8) Overtime Allowance 9) City Compensatory Allowance 10) Other Allowances: i) Shift allowance ii) Marriage allowance iii) Project allowance	1) House Rent Allowance 2) Entertainment Allowance 3) Travel Allowance 4) Special Allowance exempt u/s 10(14)(ii) a) Children Education Allowance b) Hostel Allowance c) Composite hill Allowance d) Tribal Area Allowance e) Allowance for meeting personal expenditure to an employee of transport organization while on duty during the running of such transport f) Border Area Remote Area, Difficult Area or Disturbed Area Allowance	1) Conveyance Allowance 2) Foreign Allowance 3) Allowances to High Court Judges 4) Allowance from UNO 5) Special Allowance notified U/S 10(14)(i) a) Tour allowance b) Daily Allowance c) Conveyance Allowance for performance of official duty d) Helper allowance e) Academic allowance f) Uniform allowance

5.3.10.1 Fully Taxable Allowances

Fully taxable allowances which are shown in the table received by an employee from his employer are included fully in his salary income in order to ascertain his tax – liability.

5.3.10.2 Partially Exempted Allowances

The allowances which are partially exempted and remaining part is taxable treated under this category. The taxable portion is ascertained as below.

(A) House Rent Allowance [Sec 10 (13A)]

Generally, employees receive house rent allowance from their employers to meet the expenditure incurred by them towards house rent. It is exempt from tax subject to the following limits:

Least of the following is exempt from tax:

i) Actual house rent Allowance received by the employee in respect of the relevant period; or

ii) Rent paid by the employee in excess of 10% of salary due to him in respect of the relevant period; or

iii) 50% of salary due to him in respect of the relevant period if the accommodation is situated at Mumbai, Kolkata, Delhi or Chennai; or

iv) An amount equal to 40% of the salary due to him in respect of the relevant period if the accommodation is situated at any other place.

The least amount is exempt from tax and the remaining amount shall be taxable and is included in the gross salary.

Quantum of exemption: Minimum of following three limits:

	Mumbai/Kolkata/Delhi/Chennai	Other cities
1.	Allowance actually received	Allowance actually received
2.	Rent paid in excess of 10% of salary	Rent paid in excess of 10% of salary
3.	50% of salary	40% of salary

Note:

i) Meaning of salary = Basic salary + Dearness allowance (if it is under the termsof employment) + commission at fixed rate on sale.

Illustration 12

Mr. Varun resides in Chennai. He is paid Rs. 3, 80,000 as basic salary. He also gets Rs.1, 20,000 as House rent allowance. The rent paid by him is Rs. 95,000; calculate exempt and taxable house rent allowance.

Solution:

Least of the following is exempt:	Rs.
i) Actual house rent allowance received	1, 20,000.
ii) Excess of rent paid over 10% of salary (95,000 – 38,000)	57,000
iii) ½ of salary $\frac{3,80,000}{2}$	1, 90,000

As Rs. 57,000 is the least amount, Thus, exempt house rent allowance is Rs. 57,000 thus, taxable house rent allowance = Rs. 1,20,000 – 57,000 = Rs. 63,000.

Illustration 13

Mr. Rakesh received the following emoluments from a private company during the previous year: (i) Salary @ Rs. 8,000 p.m., (ii) Dearness allowance @ 20% of salary (1/2 of it is under the terms of employment) (iii) Bonus Rs. 20,000 (iv) Commission on sale @ 5% (sales Rs. 2, 50,000) (v) House rent allowance @ Rs. 2,000 p.m. Compute the taxable House rent allowance when he:

a) Resides in a rented house @ Rs. 2,200 p.m. in Agra.

b) Resides in a rented house @ Rs. 3,000 p.m. in Delhi.

c) Resides in a house owned by his mother without paying any rent. Fair rental value of the house is Rs. 4,000 p.m.

Solution:

Salary + D.A. (under the terms of employment) + commission on sale = Rs. 96,000 (Rs. 8,000 × 12)+D.A. 9,600 (10% of D.A. under the terms of employment) +12,500 $\left(\text{Rs. } 2,50{,}000 \times \frac{5}{100}\right)$ = Rs.1, 18,100.

a) When he resides in Agra at Rs. 2,200 p.m. Least of the following will be exempted.	Rs.
i) Actual allowance received Rs. 2000 × 12	24,000
ii) (Rent paid – 10% of salary) or Rs. 26,400 – 11,810	14,590
iii) 40% of salary	47,240
Hence, Rs. 14,590 is exempt	
Taxable H.R.A. = Rs. 24,000 – Rs. 14,590	9,410

b) When he resides in Delhi at Rs. 3,000 p.m. least of the following will be exempted.	Rs.
i) Actual amount received Rs. 2,000 × 12	24,000
ii) (Rent paid – 10% of salary) Rs. 36,000 – Rs. 11,810	24,190
iii) 50% of salary	59,050
Rs. 24,000, Actual H.R.A. received is fully exempt.	

c) Taxable H.R.A.will be Rs.24,000. He will not get exemption of any amount of H.R.A. as he is not paying any rent for his residential accommodation.

B) Entertainment Allowance

It is paid by an employer to his employee to compensate his entertainment expenses. The total amount is firstly included in his salary income and at last if employee fulfills certain conditions, it is allowed as deduction. This has been explained under the head "Deductions from Salaries" in unit 6.

C) Transport Allowance

Transport allowance is taxable for normal personfrom A.Y. 2019-20 but for blind or deaf or dumb or orthopedically handicapped with disability of lower extremities, it will be exempt up to Rs. 3,200 p.m.

D) Special Allowances specifically exempted u/s 10 (14) (ii) notification No. SO 259(5) dated 27-3-1990 have notified the following allowances:

i) **Special Compensatory Hilly area allowance or High Altitude allowance or uncongenial climate allowance or show bound area allowance or Avalanche allowance** is exempt from tax up to maximum of Rs. 300 p.m. If employee is working at height 1,000 meter or above the sealevel.

The prescribed limit depends upon the height of the regions, Rs. 7,000 for Siachen area of Jammu & Kashmir or Rs. 800 p.m. for other hill areas (located at height of more than 9,000 feet).

ii) **Border area allowance or remote area allowance or difficult area allowance or disturbed area allowance** is exempt at the following rates:

a) Andaman, nicobar and narcondum islands some specified places of north, some specified places of himachal Pradesh, and areas beyond 25 km from Lungali district of Mizoram - **Rs. 1,300 p.m.**

b) Continental shelf of India and exclusive economic zone of India- **Rs. 1,100 p.m.**

c) Arunchal Pradesh, Jammu and Kashmir, district Lungali of Mizoram, Nagaland, Tripura, South Andaman, some areas of Himachal Pradesh- **Rs. 1,050 p.m.**

d) Uttar Pradesh, Haryana, Rajasthan, Punjab, Aizawal district of Mizoram, some areas of Jammu and Kashmir, Tripura, Manipur, himachal Pradesh- **Rs. 750 p.m.**

e) Jog falls in district shimoga of Karnataka - **Rs. 300 p.m.**

f) Some areas of Himachal Pradesh, throughout Assam and Meghalaya- **Rs. 200 p.m.**

iii) **Tribal allowance**

This exemption is available @ Rs. 200 per month in nine States (i) Madhya Pradesh (ii) Tamil Nadu (iii) Uttar Pradesh (iv) Karnataka (v) Tripura (vi) Assam (vii) West Bengal (viii) Bihar and (ix) Orissa.

iv) **Any allowance granted to an employee working in any transport system** to meet his personal expenditure during his duty performed in the course of running of such transport from one place to another place in India, is exempt up to a specified limit. The specified limit is 70% of such allowance or Rs. 10,000 p.m. (whichever is less)

v) **Children educational allowance:** It is exempt @Rs. 100 per month per child up to a maximum of two children.

vi) **Hostel allowance:**Any allowance granted to an employee to meet the hostel expenditure on his child @ Rs. 300 p.m. per child up to a maximum of two children.

viii) **Compensatory field area allowance:** Exempt to the extent of Rs. 2,600 permonth (Specified areas of Jammu and Kashmir, Uttar Pradesh, Himachal Pradesh, Manipur, Nagaland, specified areas of Arunachal Pradesh).

viii) **Counter insurgency allowance:** Exempt to the extent of Rs. 3,900 per month. This allowance is granted to members of armed forces operating in areas away from their permanent location for a period of more than 30 days.

ix) **Underground allowance:** Such allowance is granted to an employee who is working in uncongenial climate in underground coal mines shall be exempt to the extent of Rs. 800 per month.

x) **High altitude allowance:** Given to the members of armed forces for altitude of 9000 feet to 15000 feet Rs. 1,060 per month and altitude above 15000 feet Rs. 1,600 per month.

xi) **Special compensatory highly active field area allowance:** Such allowance is given to the members of armed forces and is Exempt upto the extent of Rs. 4,200 per month.

xii) **Island (duty) allowance:** Given to the member of the armed forces in Andaman & Nicobar and Lakshadweep Group of Islands and is exempt upto the extent Rs. 3,250 per month.

xiii) **Compensatory modified field area allowance:** Exempt upto the extent of Rs. 1,000 per month (Specified area of Punjab, Rajasthan, Haryana, Himachal Pradesh, Arunachal Pradesh, Assam, Mizoram, Tripura, Sikkim, West Bengal Uttar Pradesh, Specified Areas of Jammu and Kashmir)

5.3.11 'Profits' in Lieu of Salary

As stated above-the term salary includes any profit in lieu of salary, the above term according to Section 17(3) includes:

i) **Compensation received by an employee on termination of his employment or on modification of his terms of employment.** Compensation is basically a capital receipt since it is the very source of income i.e., the salary. Capital receipts are not taxable unless by definition they are treated as income. In the present case, the termination compensation is specifically treated as profit in lieu of salary.Such compensation is taxable as salary.

   Sometimes, the terms and conditions of employment may be modified in future; the employee will get lower salaries in lieu of which they will be paid immediately a lump sum consideration. Such payment is taxable as salary.

ii) **Payments from unrecognized fund**

   Any payment received by an assessee from an unrecognized provident fund or any fund (not being an approved superannuating fund) tothe extent it consists of employer's contribution and interest thereon is taxable as profits in lieu of salary.

Specific exemptions

The following payments, however, do not constitute profits in lieu of salary.

i) Exempted Gratuity-[Section10(10)]

ii) Exempted value of Commuted Pension-Section 10(10A)

iii) Exempted amount of Retrenchment Compensation-Section 10(10B)

iv) Payment from Statutory Provident Fund-Section 10(11).

v) Exempted amount from Recognized Provident Fund-Section 10(12).

vi) Payment from Approved Superannuation Fund-Section10(13).

vii) House Rent Allowance.

Check Your Progress A

1) Define the term ‘Salary’ as per Section 17(1) of Income Tax Act.

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2) A is a non – government employee getting a salary of Rs. 6,000. He retires and receives Rs. 4, 00,000 as gratuity after serving 25 years 8 months. The employee is covered by the Payment of Gratuity Act. Calculate exempted amount of gratuity.

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3) Mr. Rathore retires from Private Service on 30th April, 2020 and his pension has been fixed at Rs. 6,000 p.m. He gets ½ of his pension commuted and gets Rs. 3, 00,000. He also received Rs. 1, 50,000 as gratuity. He gets his pension commuted during January, 2021. Pension becomes payable on the 1st day of each month, calculate taxable pension.

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....

4) Mr. Kaushik retired from service on 31st December, 2020. His pension was fixed at Rs. 6, 000 p.m. He commutes half of his pension and received Rs. 2, 70,000. Find out taxable amount of commuted pension if:

   i) He is government employee.

   ii) He is a private employee who get gratuity

   iii) He is a private employee who did not get any gratuity.

....

....

....

5) Which of the following statements are True or False:

i) Under Section [10(10AA)], leave salary for a period up to maximum of ten months is exempt from tax.

ii) Family pension received by the wife of a deceased employee is taxable under the head 'Income from other sources'.

iii) The maximum notified exemption in respect of gratuity received by private sector employees is Rs.20,00,000.

iv) For calculating the exemption in respect of house rent allowance, all allowances are to be included in salary.

v) Interest on employee's contribution to unrecognized provident fund is chargeable under the head salaries.

vi) The maximum amount for deduction as entertainment allowance to government employee is Rs.5,000.

vii) Foreign allowance is exempted from tax.

viii) House Rent Allowance is exempted for Government Employees.

ix) Salary includes wages and pension.

x) The maximum exempted limit for Gratuity is Rs 20,00,000.

5.4 LET US SUM UP

Income from salary is one of the main heads of income. Salary means any remuneration paid by the employer to the employee for service rendered. The meaning of salary for tax purpose is very wide. It not only includes the cash received but also the monetary value of facilities and benefits attached with the office of employment. It includes salary or wages, bonus, pension, annuity, gratuity, leave encashment, advance, fees or commission, contribution to provident fund, profit in lieu of salary.

In order to calculate the taxable salary of an individual, the taxable amount of all the above items is to be calculated and added together. The term salary is not only wide but has many meaning. 'Salary' includes different items for different purpose, for example, while calculating the encashment of earned leave 'salary' means basic salary, dearness allowance if terms of employment so provide and commission, if based on fixed percentage of turnover. For calculating gratuity and HRA, 'salary' includes basic salary, DA, if terms of employment so provide, dearness pay and commission, if based on fixed percentage of turnover.

5.5 KEY WORDS

Advance against salary: This is loan availed by employee repayable in installment and is not taxable.

Advance Salary: This is salary received for services yet to be rendered, and is taxable on receipt basis.

Allowance: Monetary benefits attached to an office or employment like conveyance allowance, HRA, etc for meeting particular requirements connected with the services rendered by the employee or compensation for unusual conditions of service.

Annuity: A certain sum paid for a certain period by the employer to his employee in consideration of service rendered by him.

Arrears of Salary: This means salary due but not yet received.

Commutation of Pension: A retired employee who is in receipt of pension can choose to forego a part of his pension in future, in lieu of which, he can get a lump sum. Thisis known as commutation. Exemption is available in respect of such commutation subject to limits.

Encashment of Earned Leave: Usually, employees get 30 days of earned leave in a year which can be accumulated. Generally, all organization allows their employees to encash their earned leave, if the accumulation exceeds a prescribed limit. Leave encashed during service period is taxable while leave encashed on retirement is exempt subject to certain limits.

Gratuity: This is a lump sum payment paid to an employee, usually at the time of retirement in recognition of long and meritorious service. Exemption is available subject to certain limits.

Pension: This is a monthly payment received by a retired employee from his former employer. This is taxable as salary income.

Profits in Lieu of Salary: The Income Tax Act treats certain items like compensation received by an employee on termination of his employment, certain payment from unrecognized provident fund and all other payment made by an employer or former employer as profits in lieu of salary. These are taxable as salary income.

5.6 ANSWERS TO CHECK YOUR PROGRESS

Check Your Proegess A

2) Rs. 90,000;
3) Rs. 1, 54,000;
4) (a) fully exempt (b) Rs. 90,000 (c) Rs. Nil
5) i) True, ii) True, iii) True, iv) False, v) False, vi) True, vii) True, viii) False, ix) True x) True

5.7 TERMINAL QUESTIONS/EXERCISES

1) What are the provisions of Income Tax Act regarding commutation of pension?
2) What are the provisions for calculating House rent allowance?
3) What do you mean by profit in lieu of salary?

4) Mr. Ajay is an officer in U.P. Govt. in the pay scale of Rs. 10,000 – 500 – 16,000 since 1st June, 2020. Calculate basic salary for the A.Y. 2021-22.

[Answer: 10,000 x 2 + 10,500 x 10 =1,25,000]

5) Mr. Abhishek is getting a pension of Rs. 8,000 per month from a company. During the previous year he got his three-fourth pension commuted and received Rs. 7, 20,000. Compute the exempted amount assuming if he also received gratuity.

[Answer: Rs. 3, 20,000]

6) Mr. Sanjeev is working in a concern. His basic pay is Rs. 6,000 p.m. and dearness pay @ 10% of basic pay. Commission based on fixed percentage of turnover Rs. 25,000 for the whole year. House rent allowance is Rs. 1,200 p.m. and actual rent paid by him Rs. 1,000 p.m. House is situated in Lucknow. Compute taxable House rent allowance.

[Answer: Rs. 12,100]

7) From the following particulars, compute Mr. Jagdish's taxable amount of earned leave.

	Rs.
Basic Pay	8,000 p.m.
D.A. (Under the terms of employments)	800 p.m.
Earned Leave encashed on retirement on 31st March, 2020	2, 00,000
Completed year of service	20 years
Leave in credit	5 months

[Answer :(2, 00,000 – 44,000) = Rs. 1,56,000]

8) From the following particulars, calculate gross taxable salary of Mr. Ashish for the A.Y. 2021-22.

Basic Pay	10,000
D.A. (Under the terms of employment)	5,000
Bonus	25,000
Taxable part of Gratuity received	3, 00,000
Completed year of service	35 years
Leave consumed during service	28 months
Actual amount of leave encashment	1, 50,000

[Answer: Gross salary Rs.3, 85,000]

9) From the following particulars of Dr. Ghanshyam Das, calculate the exempted amount of gratuity. He is not covered by the Payment of Gratuity Act.

Date of retirement	30 June,2020
Gratuity received	Rs.5, 00,000
Service	30 years 11months

Basic Pay	Rs, 10,000 p.m
D.A. (Considered for retirement benefit)	Rs. 3,000 p.m.
Commission on sales	2%
Sales achieved by him	3,80,000

[Answer: Exempted amount = Rs.2,04,495]

10) Mr. Nagraj, who is not covered under Payment of Gratuity Act, retires on 25 December, 2020 from ABC Ltd. and service of 36 years 9 months and he received gratuity amount Rs 5,00,000. His salary is Rs. 6,000 per month up to June 30, 2020 and 7,000 per month from July 2020. He also gets D.A. of Rs. 1,000 per month (70% of which is considered for service benefit). Find the taxable amount of Gratuity for the A.Y. 2021-22.

[Answer: Rs. 3,70,400]

11) Mr. Azad is an employee of Vijaya Steal Company in Delhi. He draws a basic pay of Rs. 12,000 p.m. and D.A. 8,000 p.m. which is considered for computation of retirement benefits. He earns 3% commission on sales achieved by him. The turnover achieved by him during F.Y. ended 2020-21 is Rs. 8,00,000. He is getting H.R.A. of Rs. 8,000 p.m. He pays rent of Rs. 8,000 p.m. calculate his gross salary for A.Y. 2021-22.

[Answer: (1,44,000+96,000+24,000) = 2,64,000+Taxable H.R.A. 26,400= 2,90,400]

12) Sri Amar is an employee in a company of Chennai. Following are the particulars. Rs.

a)	Basic Salary	7,000 p.m.
b)	D.A. (under the terms ofemployment)	1,000 p.m.
c)	H.R.A.	1,200 p.m.
d)	Rent actually paid	1,500p.m.

e) He retired on 1st January, 2020 after completing 25 years of service. The company paid him Rs. 4,50,000 as gratuity. He is not covered under the payment of gratuity act. The company paid him Rs. 5,000 p.m. as pension.

f) Salary and pension become due on the last day of each month. Compute gross salary of Sri Amar.

[Answer: Taxable H.R.A. = (Rs 10,800 – Rs 6,300) = Rs 4,500

Taxable Gratuity = (Rs 4,50,000 – Rs 1,00,000) = Rs 3,50,000

Gross Salary (63,000+9,000+15,000+4,500+3,50,000) = Rs. 4,41,500]

Note: These questions will help you to understand the unit better. Try to write answer for them. But do not submit your answers to the University. These are for your practice.

UNIT 6 SALARIES-II

Structure

6.0 OBJECTIVES

After going through this unit, you should be able to:

- define the term 'perquisite';
- list different types of perquisites made available to salaried employees;
- compute the value of such perquisites; and
- explain statutory deductions available to a salaried employee.

6.1 INTRODUCTION

In Unit 5, you have learnt about the items to be included under the head 'Salaries', you will also study about allowances which are nothing but perquisites received in cash. In this Unit, you will learn about certain perquisites which are received in kind and can be converted into cash. You will also learn about the valuation of these perquisites and the deductions available from salaries.

6.2 PERQUISITES

Perquisites are casual emoluments or benefits, which is made available to employees in addition to normal salary or wages. Perquisites may be either in cash or in kind, normally, they are in the form of facilities in kind. The basic concept underlying taxation of perquisites is that it results in a personal advantage to the recipient.

You know that 'perquisite' is a component of salary income. It follows, therefore, that there should exist 'employer-employee relationship', before the item of perquisite can be brought to tax as salary. The value of any perquisite to a person, not arising out of employer-employee relationship is taxable as 'income from other sources'. Thus, tips received by waiters from customers are taxable as 'income from other sources'.

It is important that the advantage arising to the employee should have a legal basis. Any unauthorized advantage taken by the employee would not amount to a benefit or advantage [C.I.T. v A.R. Addaikkappa Chettiar (1973) 19 ITR 90 (Mad) and C.I.T. v Kulandaivelu Konar (1975) 100 ITR 629 (Mad).] Suppose A Ltd., allots a bungalow to one of its general manager. Subsequently, he resigns from the company. However, he continues to live in the company's bungalow for a year after which he was evicted from the premises through legal proceedings. Now, the question arises as to whether any perquisite arises in the hands of the general manager, the value of which would be charged as salary in his hands.

It is a fact that he enjoys the possession of the bungalow which does entail some cost to the company and hence, there arises a perquisite. In the absence of an employer-employee relationship, it is logical to assess the perquisite value as 'income from other sources'. Sometimes, the employees to whom a perquisite is provided may waive it, instead of utilizing it. In this case, value of the said perquisite cannot be assessed in his hands.

6.2.1 Definition of Perquisites [Section 17(2)]

As per section 17(2) of the Income Tax Act, 1961 "Perquisite includes"

i) The value of rent – free accommodation provided to the assessee by his employer.

ii) The value of any concession in the matter of rent respecting any accommodation provided to the assessee by his employer;

iii) The value of any benefit or amenity provided free of cost or at concessional rate in the following cases. Anyone who fulfill any one of the following condition is called as specified employee:-

   a) By a company to an employee who is director thereof.

   b) The employee has acquired at least 20% or more equity shares in employer's company, or the employee has substantial interest in employer's company.

   c) By any employer to an employee to whom the provisions of a) and b) above do not apply but whose income under the head 'salaries' (whether due from or paid or allowed by one or more employers) exclusive of value of all benefits or amenities not provided for by way of monetary payment exceeds Rs. 50,000. In other words, an employee whose monetary salary exceeds Rs. 50,000.

iv) Any sum paid by the employer in respect of any obligation which, but for such payment, would have been payable by the assessee.

v) Any sum payable by the employer, whether directly or through a fund, other than a recognized provident fund or an approved superannuation fund, or a deposit linked insurance fund, to effect an assurance on the life of the assessee or to effect a contract for an annuity.

vi) The value of any specified security or sweat equity shares allowed or transferred directly or indirectly by the employer or former employer free of cost or at concessional rate to the assessee;

vii) The amount of any contribution to an approved superannuation fund by the employer in respect of the assessee to the extent that it exceeds Rs. 1,50,000;

viii) The value of any other fringe benefit or amenity as may be prescribed.

6.2.2 Types of Perquisites [Section 17(2)]

On the basis of taxability, perquisites may be classified into following categories:

a) Perquisites taxable for all employees (General Perquisites)

b) Perquisites taxable for specified employees

c) Tax-Free perquisites for all employees

Let us now list the items included in the above categories of perquisites.

a) Perquisites Taxable for all categories of employees (General Perquisites)

These perquisites are provided by the employer to any type of employee (Government, semi-government or employed in private undertakings) or to employees of any category. Such types of perquisites are given below:

1) Rent-Free house or accommodation:

The value of rent-free accommodation provided to the assessee by his employer is taxable perquisite in the hands of every employee. The house provided by the employer may be owned by him or may have taken some accommodation on rent for providing it to his employee.

2) Concessional rent free house or accommodation:

The employer may provide the accommodation to his employees charging less amount of rent or deducting some amount of rent from his salary. It is called concessional rent-free house.

3) Payment of employee's obligations by employer:

Such obligation can be paid in two ways, first, directly by employer on behalf of the employee, second, the employee may make payment first himself and then these are reimbursed by the employer.

The actual amount of such payment is taxable perquisite in the hands of the employee and is included in his income from ‘Salaries’. Such obligations may be of the following types:

i) Payment of employee’s personal loan.

ii) Payment of employee’s hotel or club bills, but if an employee becomes the member of a club or spends in a hotel for the benefit of his employer; this will not be treated as perquisite in the hands of the employee.

iii) Payment of education fees or other expenditure in connection with the education of employee’s children.

iv) Payment of income tax on employee’s salary.

v) Payment of salary to the domestic servants engaged by an employee.

vi) Payment of employee’s personal and legal expenses.

vii) Payment of gas, electricity or water for household if connection is in the name of the employee.

viii) Medical expenses reimburses in excess of Rs. 15,000.

ix) Premium paid for life insurance or an annuity of the employee.

x) Payment of employment tax or professional tax of the employee by the employer.

Note: Any perquisite, benefit or facility, bills of which are issued in the name of employee and the payment there of is made by the employer, shall fall under this category, i.e. payment of employee obligation and therefore, shall be included in the employee’s income from ‘salaries’.

4) Payment of employee’s life insurance and annuity premium:

The amount payable by an employer, directly or indirectly, for the assurance of the life of an employee or to effect a contract of an annuity, would be taxable perquisite in the hands of every such employee. Such premium may be paid/payable by the employer directly or through any fund other than the following funds:

i) Recognized provident fund.

ii) Approved superannuation fund.

iii) Deposited linked insurance fund established under Section 3G of the Coal Mines Provident Fund and Miscellaneous Provisions Act, 1948.

But any premium paid or payable by the employer under Employee’s state insurance scheme, would not be perquisite in the hands of the employee and shall not be taxable for the employee as this scheme is in the interest of the employee. It should be noted that the amount becomes taxable as soon as it becomes due for payment. Actual payment during the previous year is not necessary.

5) **Specified security or sweat equity share allotted or transferred to an employee:**

The value of any specified security or sweat equity shares allotted or transferred directly or indirectly, by the employer or former employer, free of cost or at concessional rate to the assessee, would be taxable in the hands of every such employee and included in the income from salaries.

6) **Employer's contribution to an approved superannuation fund:**

Any amount contributed by the employer in employee's approved superannuation fund in excess of Rs. 7, 50,000 would be taxable as perquisite. [Sec 17(2) (vii)]

7) **Fringe Benefits**

Prescribed fringe benefits or amenities are as follows:

i) Interest free loan or concession loan to an employee [Rule 3(7)(i)]

ii) The value of travelling, touring and any other expenses paid for or borne or reimbursed by the employer to the employee or any member of his household.

iii) Free food, non-alcoholic beverages or refreshment facilities. [Rule 3(7)(iii)]

iv) Any gift or voucher or token. [Rule 3(7) (iv)]

v) Credit card facility [Rule 3(7)(v)]

vi) Club expenditure [Rule 3(7)(vi)]

vii) Use by an employee or any member of his household of any moveable asset belonging to the employer.[Rule 3(7)(vii)]

viii) Transfer of employer's moveable asset to an employee or any member of his household. [Rule 3(7)(viii)]

ix) Any other benefit, amenity, service, right or privilege provided by employer [Rule 3(7) (ix)]

b) **Taxable Perquisites for specific employees [Section 17(2)(iii)]**

According to section 17(2) (iii) of the Act, Perquisites which are taxable in the hand of specified employees only, are called as specific perquisites.

Meaning of a Specified Employee:

A person who fulfills any one of the following condition shall be considered as a specific employee:

i) If the employee is a director in employer's company – full time or part time.

ii) The employee has acquired at least 20% or more equity shares in employer's company or the employee has substantial interest in employer's company.

iii) The total monetary receipts of an employee must exceed Rs. 50,000. An employee (not covered under any of the above two categories) whose taxable 'monetary income' under the head 'salary' (excluding the value of non-monetary perquisites) exceeds Rs. 50,000 is a specified employee. In case an employee gets salary from more than one employer, he will be treated as specified employee, if the aggregate monetary salaries from all the employers exceed Rs. 50,000.

'Monetary salaries income' includes all taxable cash receipts e.g., basic salary, dearness allowance, bonus, commission, taxable allowance, obligations of employee paid by employer, e.g.- income tax, employment tax, payment of gas, electricity and water and also received at the time of retirement, e.g., taxable gratuity, encashment of earned leave or sum received from provident fund, etc.

Name of specific perquisites, taxable in the hands of specific employees

1) Facility of motor car.
2) Facility of domestic servants

   (Sweeper, Gardner, Watchman, or Personal Attendant) for the personal works of an employee employed and engaged by the employer and paid by the employer.
3) Facility of free gas, electricity and water
4) Free education facility provided by the employer to the children of an employee in a school run by the employer or in some other school.
5) Personal or private journey provided free of cost or at concessional rate to an employee or member of his household.
6) The value of any other benefit, amenity, service, right or privilege provided by the employer.

c) Tax – Free Perquisites for all employees

i) Medical facility
ii) Facility of refreshment
iii) Transport facility or conveyance facility
iv) Employer's contribution
v) Use of laptop or computer of employer
vi) Facility of entertainment
vii) Accommodation in remote area
viii) Perquisites provided outside India
ix) Facility of telephone
x) Facility of refresher course or training
xi) Payment of accidental insurance premium
xii) Educational facility for children of the employee
xiii) Tax paid by the employer on non-monetary perquisites
xiv) Leave travel concession
xv) Free conveyance facility to employees by an undertaking engaged in transport business
xvi) Facility of residence and conveyance to high court/Supreme court judges.
xvii) Facility of rent free accommodation to minister of parliament (including maintenance).

6.3 VALUATION OF PERQUISITES – ALL EMPLOYEES

For the purpose of computing the income chargeable under the head 'Salaries', the value of the perquisites, not provided by way of monetary payment to the assessee shall be determined in accordance with the provisions of Rule 3 of Income Tax Rules, 1962.

6.3.1 Rent Free Accommodation – Rule 3(1)

As per rule 3(1), for the purpose of valuation of rent-free accommodation, all employees are divided into two categories.

1) A) **Government employees:** The following are included under this category:

   a) Employees of Central and State Governments.

   b) Government employees on deputation and presently serving with any body or undertaking under the control of Government. Foreign Government employees are not included in this category. They are included in the second category.

   B) **Other than Government employees:** All employees not covered under first (A) category are included under this category.

   Types of Rent free accommodation: The accommodation provided by the employer to his employee may be of one of the following two categories:

   i) *Unfurnished accommodation* – The accommodation which in not fitted with any furniture or other things of amenities is termed as unfurnished.

   ii) *Furnished accommodation* – The accommodation which is equipped with furniture or other things of amenities such as television, refrigerator, air conditioning plant or equipment and other domestic appliances, etc. is termed as furnished.

   Further, such accommodation may be provided.

   a) Rent free, or

   b) At concessional rate

2) **In case accommodation provided by Government to its employees**

   i) **Where the accommodation is unfurnished**: The value shall be the license fee determined by Union or State Government is respect of accommodation in accordance with the rules framed by that government as reduced by the rent actually paid by employee.

   Valuation = License fee determined by Central or State Government in respect of accommodation in accordance with the rules framed by that government – Rent actually paid by the employee.

   ii) **Where the accommodation is furnished**: The value of perquisite shall be determined as if it is an unfurnished accommodation (i.e. value determined as per clause (i) above). Such value shall be increased by 10% of the cost of furniture (including television, radio, refrigerators, other household appliances, air conditioning plant or equipment) or if such furniture is hired from third party, the actual hire charges paid or payable for the same. The valuation of furniture shall be reduced by any charges paid or payable for such furniture by the employee during the previous year.

Valuation = as unfurnished + 10% of the cost of furniture installed in the accommodation (if the furniture is owned by the Government)
Or
Actual rent or hire of furniture installed in the accommodation paid by the Government (if the furniture installed in the accommodation has been taken on hire by the Government)

Note:

1) Meaning of salary = Basic salary due (except advance and arrears of salary) + Dearness allowance or pay (if under the terms of employment) + fees + bonus and commission + all other taxable allowances (excluding the portion not taxable) + any monetary payment (by whatever name called), but does not include the following:

   a) Dearness Allowance or Dearness Pay (which in not under the terms of employment)

   b) Employer's contribution to assessee's Provident Fund.

   c) Exempted Allowances

   d) Value of any Perquisites under section 17(2).

   e) Any payment or expenditure specifically excluded under proviso to sub clause (iii) of clause (2) relating to employees stock option plan or scheme) or proviso to clause (2) of section 17 (relating to medical facility or reimbursement of medical expenses);

   f) Any lump sum payment like Gratuity, Leave Encashment, Commuted Pension, etc, received at time of termination of service or at the time of voluntary retirement or superannuation.

2) 'Accommodation' includes a house, flat, farm house, or part thereof, or accommodation in a hotel, motel, service apartment, guest house, caravan, mobile home, ship or other floating structure.

3) Rent free official residence provided to a judge of a high court or to a judge of the Supreme Court is exempt from tax.

4) Rent free accommodation given to an official of parliament, a union minister and a leader of opposition in parliament is exempt from tax.

Illustration 1

Mr. Y. is an I.A.S. Officer in the Ministry of Home Affairs, New Delhi. He draws a basic pay of Rs. 12,000 p.m. and dearness allowance of Rs. 1,200 p.m. He is provided a rent free house at Jor Bagh, the fair market rent of which is Rs. 72,000 p.a., Bonus – 3 months' basic pay; education allowance @ 6,000 p.m.; city compensatory allowance @ 6,000 p.m.; cost of furniture – Rs 50,000; license fee determined by the government – Rs 12,000 p.a. Determine the value of rent-free accommodation if the house is (i) unfurnished (ii) furnished and hire charges of furnishing are Rs. 2,000 p.a.

Solution:

i) Mr. Y (Government employee - unfurnished)

Valuation for rent free house = License fee determined by the Government = Rs. 12,000.

Note:

1) License fee determined by the Government is Rs. 12,000 p.a. Hence, Rs. 12,000 shall be the value of rent free accommodation.

2) Market rental value of the accommodation and the salary of the employee are irrelevant for valuation and rent free accommodation of a Government employee, when license fee is given.

ii) Mr. Y (Government employee - furnished)

Valuation for rent free house = License fee determined by the Government + hire charges of furnishing.

= Rs. 12,000 + 2,000 = Rs. 14,000

B) In case accommodation is provided by any other employer

Accommodation provided as rent free or at concessional rate may be owned by the employer or taken on lease or rent by the employer.

It includes other employees like employees of Reserve bank of India, nationalized banks, educational institutions, universities, statutory corporations, companies of private sector, partnership firms and other industrial and trading institutions etc.

The taxable value of this facility shall be determined as follows:

1) Where the Accommodation is Unfurnished

Table 6.1: Unfurnished Accommodation

Nature of Accommo-dation	Accommodation provided in cities having population upto 10 lakh as per 2001 census	Accommodation provided in cities with population exceeding 10 lakhs but not exceeding 25 lakhs as per 2001 census	Accommodation provided in cities having population exceeding 25 lakhs as per 2001 census
(a) Where the accommodation is owned by the employer	7.5% of salary in respect of the period during which the said accommodation was occupied by the employee during the previous year.	10% of salary in respect of the period during which the said accommodation was occupied by the employee during the previous year.	15% of salary in respect of the period during which the said accommodation was occupied by the employee during the previous year.
(b) Where the accomm-odation is taken on lease or on rent by the employer	Actual amount of lease or rent paid or payable by the employer or 15% of salary, whichever is less	Actual amount of lease or rent paid or payable by the employer or 15% of salary, whichever is less	Actual amount of lease or rent paid or payable by the employer, or 15% of salary, whichever is less.

Explanation:

1) In case, the house is provided at concessional rate, the value determined as per (a) or (b) above shall be reduce by the rent, if any, actually paid by employee.

2) Where the Accommodation is furnished: The value of perquisite shall be determined as if it is an unfurnished accommodation (i.e. value determined as per chart given above. Such value shall be increased by 10% of the cost of furniture (including television, radio, refrigerators, other household appliance, air conditioning plants or equipment or other similar appliance or gadgets) or if such furniture is hired from a third party, the actual hire charges payable for the same. Such valuation of furniture shall be as reduced by any charges paid or payable for such furniture by the employee during the previous year.

> **Valuation** = Valuation as unfurnished accommodation + 10% of the cost of furniture
>
> Or
>
> Valuation as unfurnished accommodation + actual rent or hire charge of the furniture paid by the employer (if furniture is taken on lease or hire)

C) Where the accommodation is provided by the employer (Govt. or other employer) in a hotel

The value of the accommodation shall be –

i) 24% of salary paid or payable for the previous year, or

ii) The actual charges paid or payable to such hotel, whichever is lower, for the period during which such accommodation is provided. However, if the employee pays any rent, the value so determined shall be reduced by the rent actually paid or payable by the employee.

There will be no perquisite value, if the accommodation is provided in a hotel if the following two conditions are fulfilled:

a) Such accommodation is provided for a period not exceeding 15 days; and

b) It has been provided on the transfer of the employee from one place to another.

> **Valuation** = 24% of salary paid or payable for relevant period of the previous year
>
> Or
>
> Actual charge paid or payable by the employer to such hotel, whichever is less. (Such accommodation is treated as furnished)

Note: For the purpose of valuation of rent-free accommodation, the following should be understood clearly:

1) Meaning of Salary – Salary for this purpose is to be taken as salary of the period for which rent free accommodation is given to the employee. Salary means and includes the following:

a) Basic salary

b) Dearness Allowance or Dearness Pay, if it is under the terms of employment. All the allowances paid by the employer to the employee on monthly basis or otherwise, such as fees, bonus, commission, dearness allowance or dearness pay (if it is under terms of employment) and all other taxable allowances (excluding the portion not taxable)

c) Bonus

d) Commission

e) Any monetary payment (by whatever name called)

But, the following are not included in the salary:

i) Dearness Allowance or Dearness Pay, if it is not under the terms of employment.

ii) Employer's contribution to provident fund account of the employee

iii) All Allowances exempt from income tax.

iv) Value of any Perquisite u/s 17(2).

2) "Accommodation" includes a house, flat, farm house or part thereof, or accommodation in hotel, motel, service apartment, guest house, caravan, mobile home, ship or other floating structure.

3) "Hotel" includes licensed accommodation in the nature of motel service apartment or guest house.

4) Salary is to be computed on 'due' basis for the period for which the rent free accommodation has been provided to the employee e.g., if the rent free accommodation is provided for the period from 1.1.2021 to 31.3.2021, then only the salary due for the months of January, February and March shall only be taken.

5) If the employee receives salary from more than one employer, the aggregate of the salary received from both the employers, for the period for which the accommodation is provided, has to be taken into account for valuation of rent free accommodation even though the accommodation has been provided only by one employer.

Illustration 2

A is a pilot in Air India. He draws Rs. 72,000 p.a. as basic pay, Rs. 12,000 p.a. as D.A. (it is under terms and conditions), Rs. 6,000 as bonus and Rs. 6,000 p.a. as educational allowance. He has got two children studying in the nearby school. While on duty, he has been provided with a rent-free flat at Santa Cruz, Mumbai, the fair rental value of which is Rs. 30,000 p.a. Determine the taxable value of the perquisite if

i) The house is unfurnished

ii) The house is furnished and the cost of furnishing is Rs. 1,00,000/-

Solution:

i) When accommodation is unfurnished

Valuation = 15% of salary

Total salary = 93,600

15% of salary (As population of Mumbai is above 25 lakhs) = Rs 14,040

Note:

1) Meaning of salary = 72,000 (B.S.) + 12,000 (D.A.) + 6,000 (B) + 3,600 (E.A.) = Rs. 93,600

2) D.A. is under terms of conditions so it will be included.

3) Education allowance is exempt upto 100 p.m. per child (maximum two children, i.e. 2,400 is exempt). Taxable portion of education allowance and all other allowances will be included in salary.

ii) When accommodation is furnished

Valuation = 15% of salary + 10% of cost of furniture

= 14,040 + 10,000 = 24,040

Note:

Salary = Rs. 93,600 (15% of Rs 93,600 = Rs 14,040)

Cost of furniture = Rs. 1, 00,000

Illustration 3

Mr. Ajay Dubey is a General Manager in a M.N.C. He gets Rs. 25,000 p.m. as salary, Rs. 1,500 p.m. as marriage allowance, Rs. 2,000 p.m. children allowance and Rs. 1,500 p.m. dearness allowance (of which half the amount is added in salary to ascertain the contribution to Provident Fund.). He also gets a transport allowance for commuting from residence to office @ Rs. 400 p.m. Besides, he gets a bonus equal to 3 month's basic pay per year. The company has provided him a rent free bungalow in which air conditioning plant, refrigerator, radio set and other furniture of the cost of Rs. 1,60,000 belonging to the company, are installed. The monthly rent of the bungalow payable by the company is Rs. 7,000 p.m. Calculate the Rent free accommodation value of the bungalow.

Solution:

As the bungalow is not owned by the company, the valuation of rent free furnished bungalow will be as under.

Valuation = Lease or rent paid or payable or 15% of salary (whichever is less) + 10% of the cost of furniture.

= [Rs. 84,000 or 15% of Rs. 4, 30,800] + 10% of Rs. 1, 60,000

= [Rs. 84,000 or Rs. 64,620] + Rs. 16,000

= [Rs. 64,620 + Rs. 16,000 = Rs. 80,620]

Note:

1) For this purpose, salary will include one half of the dearness allowance as it is deemed to be under the terms of employment. Thus, salary will be Rs. 4,30,800 [Rs. 3,00,000 (salary) + Rs. 18,000 (marriage allowance)+Rs. 24,000 (children allowance) + Rs. 9,000 (D.A.) + Rs. 4,800 (T.A.) + Rs. 75,000 (bonus)]

2) Marriage Allowance and Children Allowance are fully taxable.

6.3.2 Accommodation at Concessional Rent

When the accommodation is provided to the employee at a concessional rate of rent, the value of such accommodation is determined as if the accommodation was provided free of rent.

From the value, the rent paid or payable by the employee for the period during which he occupied the house during the previous year, should be deducted. The resulting amount will be added to the salary as value of concession. Generally, the employer deducts a fixed sum from the salary of his employee towards the rent of the accommodation provided to him. The sum deducted as rent is less than the actual fair rental value of the accommodation. If the employee pays fair rent of the accommodation, it cannot be said that he is receiving any concession in the matter of rent. There would be no perquisite in such a case. But, when the rent paid by him or deducted from his salary is less than the fair rental value of the accommodation, he is said to have received concession in the matter of rent. This would be a perquisite. Generally, 20% of salary or 15% of salary, as the case may be, is taken to be fair rent of the accommodation. The accommodation provided to an employee at concessional rent may be either furnished or unfurnished. Concession in rent will be valued as below:

A) In case of an unfurnished accommodation provided by an employer other than the Central Govt. or any State Government:

a) Where the accommodation is owned by the employer:

Value of Concession in rent = 15% or 10% or 7.5% of salary (as the case may be) – Rent recoverable from, or payable by the assessee

b) When the accommodation is taken on lease or hire by the employer:

value of Concession in rent = Actual lease or rent paid or 15% of salary, (whichever is less) – Rent recoverable from the assessee

B) In case of an unfurnished accommodation provided by the Central or any State Government-

Value of concession in rent =
License fee determined – Rent recoverable from the assessee

C) In case of a furnished accommodation provided by the Central or any State Government-

Value of concession in rent = License fee determined + 10% of the cost of furniture – Rent (or charges for furniture recoverable from the assessee)

D) In case of a furnished accommodation provided by an employer other than the Central or any State Government –

a) Where the accommodation is owned by the employer:

Value of concession in rent = Value as unfurnished + 10% of the cost of furniture or rent (charges for furniture Recoverable from the assessee)

b) Where the accommodation is taken on lease or rent by the employer:

Value of concession in rent = Value as unfurnished + 10% of the cost of furniture – Rent or charges for furniture recovered from the assessee

E) In case of an accommodation provided by the employer in a hotel –

Value of concession in rent = 24% of salary or Actual charge of hotel paid (Whichever is less) – Rent recoverable from the assessee

Note:

1) If accommodation in hotel is provided for 15 days or less, its value shall not be taxable.

2) Value of furniture installed in an unfurnished accommodation, 10% of the cost of furniture or actual hire charge of the furniture, if furniture is taken on hire.

In brief, value of concession in rent will be calculated as below.

For all category of employees

Value of concessional Rent free accommodation (Furnished & unfurnished)	=	Valuation as rent free accommodation	–	Rent paid or payable by or deducted from the employee

Table 6.2: Valuation of Rent Free House

Unfurnished	Government employees	Private sector employees	
	License fee determined by the government	**Accommodation owned by the employer:** a) 15% of salary (in cities with population exceeding 25 lakhs) Or b) 10% of salary (in cities with population exceeding 10 lakhs but not exceeding 25 lakhs) Or c) 7.5% of salary (in other cities)	**Accommodation hired by the employer:** Hire charges or rent paid or payable Or 15% of salary (whichever is less) (In respect of all cities)
Furnished (for all employees)	Valuation as unfurnished + 10% of the cost of furniture or actual rent or hire of the furniture paid by the employer		

6.3.3 Fringe benefits

Prescribed fringe benefits or amenities are as follows:

1. Interest free loan or concession loan to an employee [Rule 3(7)(i)]

Following points shall be kept in mind:

i) The loan shall be given to the employee or his family member (Spouse, children and their spouses, Parents, Servants and dependents) by his employer or on his behalf in the previous year.

ii) Interest shall be calculated on the maximum outstanding monthly balances.

iii) The taxable value of the loan shall be the sum equal to the interest calculated at the rate charged per annum by State Bank of India on 1st day of previous year.

iv) No value is taxable, if the loan is taken for the treatment of diseases specified in Rule 3A.

v) If the total amount of loan does not exceed Rs 20,000, it shall not be included in employee's salary.

Note:

a) The rate of interest for such loans is given by State Bank of India for every financial year.

b) Maximum outstanding monthly' balance means the aggregate outstanding balance for each loan as on the last day of each month.

Illustration 4

Determine the taxable value of taxable interest in case of interest free loan provided by the employer to the employees for assessment year 2021-22.

a) An employer, Ambani Ltd, gives the following interest free loan to Mr Amit, an employee of the company, Rs 10,000 for children education and Rs 6,000 for purchasing a washing machine. No other loan is given by Ambani ltd. Compute taxable value of interest.

b) Ambani Ltd gave loan to Mr Amit on 1st April, 2020 to buy a car of Rs 50,000. Ambani Ltd recovers interest @ 2.90% per annum from Mr Amit. Find out taxable value of interest.

Solution:

For the assessement year 2021-22, the taxable value of interest free loan shall be following:

a) Nothing is taxable in the hands of Mr Amit as the amount of loan does not exceeds Rs 20,000.

b) The SBI lending rate on April, 2020 for car loan is 9.25%, but only 2.90% interest is recovered from Mr Amit, i.e. Rs 3,175 @ interest 6.35% (9.25% - 2.90%) on Rs 50,000 for one year is taxable in the hands of Mr Amit.

2) **The value of travelling, touring and any other expenses paid for or borne or reimbursed by the employer to the employee or any member of his household [Rule 3(7) (ii)].**

Sometimes, the expenses incurred for holidays tour by the employee or his family member is reimbursed by the employer. The following points shall be kept in mind:

Table 6.3: Conditions and Taxable value for travelling and touring

Conditions	Taxable value
If all employees are provided similar type of facilities.	Expenses borne by the employer *minus* Sum recovered from the employee
If all employees are not provided similar type of facilities.	Value of facilities provided by other agencies *minus* Sum recovered from the employee.
If the employee is on official tour work and these expenses are paid for any member of his household who went with him.	Sum paid by the employer
If the employee is on official tour and this tour is extended in the form of holidays.	The expenses paid by the employer during the extended period.

Note:

i) In all above conditions, if any amount is recovered from the employee, it will be deducted from taxable value of fringe benefit and the remaining amount will be treated as the value of that particular amenity.

ii) The remaining value shall be taxable only if it is positive.

3) **Free food, non-alcoholic beverages or refreshment facilities. [Rule 3(7)(iii)]**

Following points shall be kept in mind:

Table 6.4: Conditions and taxable value for food and beverages

Conditions	Taxable value
If free tea and snacks is provided during office hours.	Nil
If free meal and non-alcoholic beverages are provided during office hours in remote area or offshore place.	Nil
If free meal and non-alcoholic beverages are provided during office hours at place of work.	i) If the rate of meal is upto Rs. 50 per meal, the taxable value shall be zero. ii) If the rate of meal exceeds Rs 50 per meal, this excess value shall be taxable.
If free meal is provided during office hours at place of work through non-transferable paid vouchers.	The taxable value shall be the sum exceeding Rs 50 per meal.
In any other case	Actual expenditure by the employer *minus* Sum recovered from the employee.

Note:

i) Office hours include over time and work in holiday.

ii) Free meals include meal, tea and snacks.

iii) Lunch allowance and free meal are separate; the value of lunch allowance, dinner allowance, refreshment allowance shall be taxable.

Illustration 5

An employer provides tea/coffee to his employee Mr Rajiv during the office hours costing Rs 5,500 in a year which is borne by the employer. Besides this, he also provides free lunch to him during office hours. The cost of this lunch for 300 working days in a year is Rs 100 per diet. The employer recovers Rs 40 per diet from his employee. Find the taxable value of this facility.

Solution:

i)	Taxable value of tea or coffee shall be nil as it is provided during the office hours.		Rs.
ii)	Taxable value of lunch (300 × 100)		30,000
	Less: i) Tax free amount (300 × 50)	15,000	
	ii) Recovered from Mr Rajiv (300×40)	12,000	27,000
	Taxable value of lunch		**3,000**

4) Any gift or voucher or token. [Rule 3 (7) (iv)]

Following points shall be kept in mind:

i) Gift can be in cash or kind.

ii) Gift can be given by the employer to his employee or any member of his family.

iii) If the cost of gift (given on any ceremonial occasion) exceeds Rs 5,000, then, it shall be taxable.

iv) Cash gift or any gift which can be converted into money (e.g. Cheque), is not exempt, but, its value shall be included in employee's salary even its value is less than Rs 5,000.

v) Any gift given by the employer to the employee on the social and religious functions (e.g.- Deepawali, Christmas, New Year, Holi etc.), if it is given in kind, it is exempt, and not included in employee's salary provided its value is not more than Rs 5,000 per year. If the value of gift exceeds Rs. 5,000, this excess value shall be taxable and included in employee's salary.

5) Credit card facility [Rule 3 (7)(v)]

It's taxable value is calculated as follows:

Total expenses paid by the employer

Less: i) Expenses in connection to office or duty

ii) Sum recovered from the employee

Expenses on credit card for official use:

For deduction in these expenses, following conditions are to be fulfilled:

i) The employer will keep complete details in connection with these expenses, e. g, date of expense, nature of expense etc.

ii) The employer will give a certificate for this purpose that these expenses have been paid for official purpose.

Note:

i) The employer shall give credit card to the employee or any member of his family or the expenses of credit card should be reimbursed by the employer.

ii) Expenses on credit card will not include membership fee and other fee or expenses which have been paid by the employee or any member of his family through credit card in connection with household purpose.

6) **Club expenditure [Rule 3 (7)(vi)]**

Its taxable value is calculated as follows:

Expenses done on club facility or reimbursed by the employer

Less: i) Expenses on club facility if any paid or recovered by the employee

Important point: Where such expenses are incurred wholly or exclusively for official purpose, then value of benefit would be Nil, provided the conditions specified below are fulfilled.

Note:

i) Health club and sports club facilities are provided by the employer in the company for all categories of the employees, these values shall be exempt for the employees.

ii) If such club facilities are provided for official purpose, the expenses paid on it by the employer shall be tax free for the employees but for this exemption certain conditions are essential to be fulfilled. These conditions are the same which have been mentioned in earlier point no. 5 (Expenses on credit card).

iii) Club membership fee: Initial one time deposit or fees for corporate membership, where benefit does not remain with a particular employee after employment are exempt.

7) **Use of employer's moveable assets by an employee or any member of his household. [Rule 3 (7) (vii)]**

If an employee uses the movable asset of the employer, its taxable value is calculated as follows:

Table 6.5: Taxable value of Movable Assets

Movable asset	**Taxable value of perquisite**
i) Use of computer or laptop	Nil
ii) Any other movable assets other than (i) above a) If the employer is the owner. b) If the employer has hired the asset.	10% p.a of cost of asset Rent by employer every year.

Note:

Any amount received from employee in connection with movable asset shall be deducted from the above value.

8) **Transfer of employer's moveable asset to an employee or any member of his household [Rule 3 (7)(viii)]**

The taxable value of this perquisite shall be determined as follows:

Table 6.6: Taxable value of transfer employer's Moveable Assets

Assets		Taxable value of perquisite
i.	Computer and electronic items	Written down value (WDV) of asset used by the employer for each completed year -50% of the cost to the employer for each completed year during which such asset was put to use by the employer on the basis of reducing balance method.
ii.	Motor car	WDV of asset used by the employer for each completed year-20% of the cost to the employer for each completed year during which such asset was put to use by the employer on the basis of reducing balance method.
iii.	Any other movable asset except(i) and (ii) above	Cost of asset used by the employer for each completed year - 10% depreciation on the basis of straight line method.

Note:

i) Electronic items or electric appliances includes data storages, computer, digital diaries and printers, this does not include domestic electrical appliances, viz., washing machine, microwave, oven, mixer.

ii) Other assets include those assets which are additional from point no. (i), viz., fridge, video camera.

iii) Any amount paid by employee or received from employee shall be deducted from the value of above perquisite determined on the basis of above rules.

9) **Any other benefit, amenity, service, right or privilege provided by employer [Rule 3(7) (ix)]**

If the employer provides any other benefits, right or special right to the employee, its value shall be determined on the basis of cost of employer, any payment made by the employee to attain these benefits, shall be deducted from this taxable value.

Illustration 6

The company has given Sachin a housing loan of Rs. 10, 00,000 on 01-10-2020 @ 6% interest p.a. The entire loan is outstanding till the end of the F.Y. Determine the taxable amount of interest for the assessment year 2021-22, assuming that the rate of interest on housing loan charged by the SBI is 10% p.a.

Solution:

Interest charged by SBI @ 10% p.a.

$$= \quad 10,00{,}000 \times \frac{10}{100} \times \frac{6}{12} = \text{ Rs. } 50{,}000$$

Interest charged by company $= \text{Rs. } 10,00,000 \times \frac{6}{100} \times \frac{6}{12}$

$= \text{Rs. } 30,000$

Chargeable interest = Rs. 50,000 – Rs. 30,000 = Rs. 20,000

Illustration 7

Mr. Y is employed in a private college on a monthly salary of Rs. 15,000. He took a loan of Rs. 20,000 from the college for purchasing a second hand car. Valuate the perquisite.

Solution:

Valuation = 'NIL' as the amount of loan does not exceed Rs. 20,000

Illustration 8

Mr. X took a loan of Rs. 50,000 from his employer for his personal purpose. He used the loan for repaying his old debts. What is the value perquisite?

Solution:

Valuation – 'NIL' as the rate of interest is not given. It is presumed that the employee pays full interest. Hence, it is not a perquisite.

Check Your Progress A

1) Who is a specific employee?

....

....

....

2) What does "Perquisite includes" as per Section 17(2) of the Income Tax Act, 1961?

....

....

....

3) Fill in the blanks

   1) Arrears of salary is taxable under the head '……………………..'

   2) Tax free salary received by the employee means tax will be paid by the ……………

   3) Facility of telephone for employees is …………perquisite.

   4) The taxable value of moveable assets, other than computer or laptop, is ………….. p.a of cost of asset, when the employer is the owner.

   5) When the accommodation is provided in a hotel for ……. Days, its value shall not be taxable.

6.4 VALUATION OF PERQUISITES FOR SPECIFIED EMPLOYEES

Perquisites which are taxable in the hands of specified employees are termed as "Specific Perquisites", rules regarding this are as follows:

6.4.1 Valuation of Facility of Motor-car [Rule 3(2)]

Motor-car or other mode of conveyance provided by the employer to his employee is a 'Specific Perquisite' and therefore, it is taxable in the hands of specific employee only. However, unauthorized use of company's car by director for his personal purpose could not be taken as perquisite in his hands. The provisions of the rule are stated below:

I) When motor car is owned or hired by the employer:

When the employer has provided to his employee, a motor car owned or hired by him, its valuation will be made as follows:

A) When maintenance and running expenses are borne and reimbursed by employer:

i) If the car is wholly used for official purposes, it is not supposed to be perquisite, so value shall be nil.

ii) If the car is used wholly for the private or personal purpose of the employee, its value shall be actual amount spent by the employer.

Valuation = The actual amount spent by the employer on maintenance and running of the car + salary of chauffeur, if any + Normal wear and tear @ 10% of actual cost of the car or hire charges – Amount charged from employee.

iii) If the car is used partly for official and partly for private purpose, its value shall be as follows:

Valuation = [If capacity of the engine of car is upto 1.6 liters] Rs. 1,800 p.m. plus Rs. 900 p.m. for chauffeur's facility

= [If engine capacity of car is above 1.6 liters] Rs. 2,400 p.m. Rs. 900 p.m. for chauffeur's facility

B) When maintenance and running expenses are borne by the employee.

i) If the car is wholly used for official purposes, its value shall be Nil.

ii) If the car is used wholly for private purposes, its value shall be as below:

Valuation = Expenditure incurred by the employer, hire charges or normal wear and tear of the car @ 10% of the actual cost of car + Salary of chauffeur, if any paid – Amount recovered by the employee.

iii) If car is used partly official and partly private purpose.

Valuation = [If capacity of engine of car is upto 1.6 ltr] Rs. 600 p.m. plus Rs. 900 p.m. for chauffeur facility.

= [If capacity of engine of car is above 1.6 ltr] Rs. 900 p.m. plus Rs. 900 p.m. for chauffeur facility.

II) When car is owned by the employee:

a) When maintenance and running expenses are borne by employer, it will not be treated as perquisite; its valuation shall be Nil.

b) When maintenance and running expenses are borne by employer.

i) If car is used wholly for official purpose:

It shall not be regarded as perquisite, so value shall be Nil.

ii) If car is used wholly for private purpose:

Actual expenses spent by the employer shall be the value of perquisite. This is assumed to be general perquisite and taxable for all employees.

iii) If car is used partly for official purpose and partly for private purpose.

Valuation = Actual expenses incurred by the employee – Rs. 1,800 p.m. (if car is upto 1.6 ltr. capacity) or Rs. 2,400 p.m. (if car is above 1.6 ltr. capacity) and 900 p.m. for chauffeur (any amount recovered from employee).

III) Use of more than one motor car belonging to the employer.

When more than one car are owned or hired by the employer and employee uses them for both personal and official use, the value shall be as follows:

Valuation = Actual amount spent by the employer + salary of driver, if any + normal wear and tear i.e. 10% of actual cost of car.

Table 6.7: Valuation of Motor Car

When expenses are met by the employee		
For official purpose	Not taxable	
Personal purpose (Fully taxable)	All the expenses of car like petrol, diesel, driver salary and 10% depreciation on car fully taxable If more than 1 car given then, second car deemed to use for private purpose	
Partly official partly personal purpose(some amount taxable)	Upto 1.6 ltrs Rs 600 p.m. + Rs 900 p.m. , (if driver is also provided by employer)	More than 1.6 ltrs Rs 900 p.m. + Rs 900 p.m. (if driver is also provided by the employer)
	When expenses are met by the employer	
For official purpose	Not taxable	
Personal purpose	Actual amount incurred on running and maintenance + chauffer remuneration+ 10% p.a of cost of asset + amount charged from employee	
Partly official partly personal purpose(some amount taxable)	Upto 1.6 ltrs Rs 1,800 p.m. + Rs 900 p.m. , (if driver is also provided by employer)	More than 1.6 ltrs Rs 2,400 p.m. + Rs 900 p.m. (if driver is also provided by the employer)

Illustration 9

Mr. Sanjeev Kant is manager in Roadways. He gets salary @ 25,000 p.m., value the perquisites of car under the following different circumstances:

a) The employer has provided him a car of 1.6 ltr capacity. Total expenses and drivers salary incurred by employer i.e. Rs. 18,000. Car is used for both private and official purpose.

b) The employer has provided him a 1.4 ltr capacity of car with driver only for private use. Expenses of car are Rs. 18,000. The cost of car is Rs. 5, 00,000.

c) The employer has provided with a facility of bus (50 horse power) which carries him along with other employees from home to office and back from office to home.

Solution: Rs.

Salary @ Rs. 25,000 p.m. × 12 months	3, 00,000
a) Use of 1.6 ltr car @ 1800 p.m. × 12	21,600
Salary of driver @ 900 × 12	10,800
	32,400
b) Value of 1.4 ltr car use only for private purpose = Actual expenses + salary of driver + 10% of cost of car.	
Rs. 18,000 + 900 p.m. x 12 (Rs 10,800) +Rs 50,000	
	78,800
c) This is no perquisite	

6.4.2 Free Lodging and Boarding Facility to Hotel Employees

i) **Lodging facilities:** This is taxable for all employees, and calculated as rent-free house given to an employee of private sector.

ii) **Food facilities:** The actual amount of food paid by employer and deducts the amount if recovered by employee.

6.4.3 Free Supply of Gas, Electricity and Water [Rule 3(4)]

If a facility of free gas, electricity and water is provided to the employee by the employer, the valuation of such perquisites is added in the salary of employee. Let us study its valuation under following situations:

Table 6.8: Valuation of free Gas, Electricity and Water

Situation	Value of Perquisite
a) If the employer is the manufacturer of gas, electricity and water, i.e. the employer supplies these facilities from his own resources and does not purchase from outside agencies.	Cost per unit borne by the employer shall be the taxable value of perquisite for the employee.
b) In any other situation.	Actual amount paid by the employer for these facilities to other agencies providing these facilities.

In the above situations, any amount paid by the employee or received from the employee shall be deducted from the taxable value determined as above.

Note:

i) If the connection of the above perquisite is in the name of employer, the amount of perquisite will be taxable in case of specified employee only.

ii) If the connection of the perquisite is in the name of employee, the amount of perquisite is taxable to all categories of employees (specific and non-specific).

6.4.4 Free or concessional education facilities to any member of employee's household [Rule 3(5)].

Table 6.9: Conditions and valuation of free or concessional education

Conditions	Valuation
a) Where the education Institution is itself maintained and owned by the employer.	The cost of education in a similar institution in or near the locality. However, if educational facilities are provided to the children of the employee (any other member of the household not covered here), the value of this perquisite shall be nil, if the cost of such education or the value of benefit per child does not exceed Rs. 1,000 p.m.
b) Where free education facilities for such members of employee's household are allowed in any other educational institution by reason of his being in employment of that employer.	– do-
c) Payment of fee by the employer directly to the educational institution or reimbursement of fee	Such payment or reimbursement is taxable to all types of employees (specified and non-specified both)
d) Educational facilities for family members other than employee's children	If educational facility is provided to any family member of specified employee, in the institution run by the employer, then the value of perquisite shall be the amount equivalent to fee of other institution of such level.If, it is provided in other institution, the value shall be actual expenditure spent by the employer.In case of family member of non-specified employee, the value of such perquisite shall be exempt.

However, in all the above cases, if any amount is paid or recovered from the employee on this account, the value of benefit computed above shall be reduced by the amount so paid or recovered.

6.4.5 Free Sweeper, Watchman, Gardener, or Personal Attendant etc. [Rule 3(3)]

The employer may provide the facility of household servants to the employee, which includes sweeper, chowkidar, gardener or other domestic servants like cook etc. They can be appointed either by the employer or by employee. The rules of their monetary valuation are as under:

1) **Appointment of servant by employer and payment of remuneration by the employer:**

   Servants are provided with rent house, the' owner of house being or the employer has provided the house to the employee by taking it on rent or the house is owned by the employee and the remuneration of the servant is paid by the employer. The following amounts of these facilities are included in the salary of specified employees under section 17(2) (iii).

   Sweeper, gardener, cook, watchman and other household servants: Sweeper is known as cleaning employee. In chowkidar, security man or guards are included. The taxable value of these perquisites to be included in the salary of employee will be the actual amount paid by employer to sweeper, gardener, cook, watchman and other household servants or total cost regarding these servants to the employer. But, the expenses incurred by the employer on maintaining garden, swimming pool and ground attached to the house shall not be taxable separately.

2) **Appointment of servant by employee and payment of remuneration by employer or the payment of remuneration by employee and reimbursement by employer:**

   The whole amount for every type of employee will be taxable u/s 17(2) (iv). The house may be of employee or employer or on rent basis.

6.5 FULLY EXEMPTED PERQUISITES (TAX FREE PERQUISITES)

There are certain other perquisites which are exempt in the hands of all employees.

They are as follows:

1) **Medical facility**

   A) **Medical facility in a hospital etc. maintained by the employer**

      Medical facility which is given to employee and his/her family member in hospital, dispensary and nursing home which belongs to employer is fully tax free.

   B) **Medical treatment in India**

      The following expenditure incurred by employer shall not be a perquisite:

      a) Any sum paid by employer in respect of:

      i) Actual expenditure incurred by employee on his or his family member's medical treatment in any hospital maintained by the government or any local authority or in a hospital approved by the government for medical treatment for its employees.

ii) Expenditure actually incurred by employee on his or his family member's medical treatment in respect of prescribed diseases or ailments as prescribed in Rule 3A of the income tax rules, in any hospital approved by the principal chief commissioner or chief commissioner of income tax, having regard to the prescribed guidelines. However, in this case, the employee has to attach along with his return of income, a certificate from the hospital specifying the disease or ailment for which medical treatment was required and the receipt for the amount paid to the hospital.

b) Any amount of insurance paid by the employer for insurance of the health of the employees under a scheme approved by the central government or the insurance regulatory and development authority.

c) Any reimbursement by the employer of any insurance premium paid by the employee, for an insurance for his health or the health of any member of his family a scheme approved by the central government or the Insurance Regulatory and Development Authority is also tax free perquisite.

C) Medical treatment outside India

The following expenditure incurred by employer on treatment of the employee or his family members outside India is also tax free perquisite:

a) Expenses on medical treatment of the employee or any member of his family outside India. However, such expenses shall be tax free perquisite to the extent permitted by Reserve Bank of India.

b) Expenses on stay abroad of the employee or any member of his family for medical treatment with one attendant who accompanies the patient in connection with such treatment. These expenses shall also be tax free perquisite to the extent permitted by Reserve Bank of India.

c) Travel expenses of the patient (employee or his family member) and one attendant who accompany the patient in connection with such treatment. It shall be tax free in the case of those employees whose gross total income (before including therein such travel expenditure as perquisite) does not exceed Rs 2, 00,000. In other words, if the gross total income of the employee before including the taxable medical perquisite on account of travel expenditure exceeds Rs 2, 00,000, the expenses on travel of the patient as well as of the attendant shall become taxable.

Note:

1) 'Family' for the purpose of medical facility means:

   i) The spouse and children of the employee. Children may be dependent or independent, married or unmarried.

   ii) Parents, brothers and sisters of the employee, who are wholly or mainly dependent on such employee.

2) 'Hospital' includes a dispensary, a clinic, and a nursing home.

Table 6.10 : Medical facility

A) Medical facility in a hospital etc. maintained by the employer	Medical facility which is given to employee and his/her family member in hospital, dispensary and nursing home which belongs to employer is fully tax free.
B) Medical treatment in India	The following expenditure incurred by employer shall not be a perquisite:Any sum paid by employer in respect of: i) Actual expenditure incurred by employee on his or his family member's medical treatment in any hospital maintained by the government or any local authority or in a hospital approved by the government for medical treatment for its employees. ii) Expenditure actually incurred by employee on his or his family member's medical treatment in respect of prescribed diseases or ailments as prescribed in rule 3A of the income tax rules, in any hospital approved by the principal chief commissioner or chief commissioner of income tax, having regard to the prescribed guidelines. iii) Any amount of insurance paid by the employer for insurance of the health of the employees under a scheme approved by the central government or the insurance regulatory and development authority. iv) Any reimbursement by the employer of any insurance premium paid by the employee, for an insurance for his health or the health of any member of his family a scheme approved by the central government or the Insurance Regulatory and Development Authority is also tax free perquisite.
C) Medical treatment outside India	The following expenditure incurred by employer on treatment of the employee or his family members outside India is also tax free perquisite: i) Expenses on medical treatment of the employee or any member of his family outside India to the extent permitted by Reserve Bank of India. ii) Expenses on stay abroad of the employee or any member of his family for medical treatment with one attendant who accompanies the patient in connection with such treatment to the extent permitted by Reserve bank of India. iii) Travel expenses of the patient (employee or his family member) and one attendant who accompany the patient in connection with such treatment. It shall be tax free in the case

	of those employees whose gross total income (before including therein such travel expenditure as perquisite) does not exceed Rs 2,00,000, if the gross total income of the employee before including the taxable medical perquisite on account of travel expenditure exceeds Rs 2,00,000, the expenses on travel of the patient as well as of the attendant shall become taxable.

2) **Facility of refreshment**

This exemption is provided only when refreshment is given during office hours and at place of duties.

3) **Transport facility or conveyance facility**

This shall be tax free to all types of employees, if an employer provides any vehicle or other transport or conveyance facility to the employee for the purpose of carrying him from the place of residence to the place of his duty and back to his residence. The conveyance facility to employee shall be tax free provided the enterprise is engaged in business of transport, e.g., facility of free pass to railway employees.

4) **Employer's contribution**

Employer's contribution in schemes like group insurance scheme, deferred annuity or pension shall be tax free.

5) **Use of laptop or computer of employer**

The use of laptops or computers (belongs to employer or hired by employer) by the employee or his family member, its value shall be exempted.

6) **Facility of entertainment**

This facility should be provided to employees collectively, to avail its exemption; else it shall not be tax free.

7) **Accommodation in remote area**

If the employer provides accommodation facility to such employees in remote area or offshore locality, its value shall be exempt. Such facility shall also be exempted for the employees who are employed at mining sites or oil exploration site.

8) **Perquisites provided outside India**

Such exemption is provided to Indian citizen and Government employees who are employed in foreign countries.

9) **Facility of telephone**

The payment of telephone (including mobile phones) bills installed at employee's residence by the employer is tax free. The telephone can be used for any purpose.

10) Facility of refresher course or training

Such perquisite is tax free provided the employees do the work with much skills, it includes lodging and boarding expenses for this purpose.

11) Payment of accidental insurance premium

Any payment made by the employer for insurance premium on policy taken by employer against any loss of employee, shall not be taxable.

12) Educational facility for children of the employee

The educational institutions is run by the employer or the employer has provided free educational facilities to the children of employees in another educational institution, the value of these facilities shall be exempt provided that such value should not be more than Rs 1,000 per child per month.

13) Tax paid by the employer on non-monetary perquisites

If an employer provides non-monetary perquisite and pays any tax on these, it shall be tax free and shall not be included in computing income under the head' salaries'. It should be noted that no deduction shall be allowed to the employer while computing income under the head 'profits or gains of business and profession'.

14) Leave Travel Concession (LTC)

An employer (present or former employer) may grant the facility of LTC to his employees with members of his family in connection with the journey to home town or any other place in India.

Leave Travel Concession shall be allowed for maximum two children since 1.10.1998. This rule shall not be applicable to those children whose birth before 1.10.1998 and also in case of multiple birth after one child.

The employee is entitled to exemption under section 10(5) in respect of the value of travel concession or assistance received by or due to him from his employer or former employer for himself and his family, in connection with his proceeding:

a) On leave to any place in India.

b) To any place in India after retirement from service or after termination of his service.

The exemption shall be allowed subject to the following:

i) Where journey is performed by air, maximum exemption shall be an amount not exceeding the air economy fare of the national carrier by the shortest route to the place of destination;

ii) Where place of origin of journey and destination are connected by rail and the journey is performed by any mode of transport other than by air- maximum exemption shall be an amount not exceeding the air-conditioned first class rail fare by the shortest route to the place of destination; and

iii) Where the places of origin of journey and destination or part thereof are not connected by rail and the journey is performed between such places- the amount eligible for exemption shall be:

a) Where a recognized public transport system exist, an amount not exceeding the 1st class or deluxe class fare , as the case may be, on such transport by the shortest route to the place of destination; and

b) Where no recognized public transport system exits, an amount equivalent to the air-conditioned first class rail fares, for the distance of the journey by the shortest route, as if the journey had been performed by rail.

An employee or assessee can avail exemption for any two journeys in a block of 4 years. For this purpose, the first block of 4 years was 1986-89 calendar years, the second block 1990-93 calendar year, the third block 1994-97 calendar years, the fourth block 1998-2001 calendar years and fifth block 2002-05, sixth block 2006-2009, seventh block 2010-2013, eight block 2014-2017, ninth block 2018-2021 and so on. If the assessee has not taken the benefit of this exemption of LTC in any block, whether for both journeys and one journey, he may avail the exemption of one journey in the calendar year immediately succeeding the end of the block of 4 years, mean in the fifth calendar year. In other words, maximum one journey can be carried forward.

Clarification:

i) The exemption regarding LTC can be availed for the journey undertaken while on leave during the tenure of service or even after retirement from service.

ii) If the journey is not performed after taking LTC, the entire amount received by employee shall be taken from him.

iii) The family of the employee includes i. the spouse and children of the employee, parents, brother, sister of the employee who is wholly dependent upon him.

iv) In any case, no exemption shall be allowed exceeding the actual amount spent on travel by the employee.

v) If the travel is performed after retirement from service or being on leave during the service, the benefit of exemption may be availed.

vi) The exemption is allowed only in respect of fare. Expenses incurred on porterage, conveyance from residence to the railway station/airport/ bus stand and back, boarding and lodging' or expenses during the journey will not be qualified for exemption.

vii) Exemption is available in respect of shortest route, where journey is performed from the place of origin to different places in a circular form or in any other manner, the exemption for that journey will be limited to what is admissible for the journey from the place of origin to the farthest point reach, by the shortest route.

15) Accommodation to judge

Rent free official residence provided to High Court or Supreme Court judges is tax free perquisite.

16) Free accommodation to ministers, etc

Rent free furnished residence, including maintenance, thereof, provided to a Union Minister, an officer of Parliament or to an Opposition Leader in Parliament is regarded as tax free.

17) Scholarship to employee's children

Scholarship given by the employer to the children of an employee is a tax free perquisite.

18) Use of health club, sports or similar facility provided uniformly to all employee by employer.

19) Conference

Any expenditure incurred by the employer for an employee in connection with a conference, such as conveyance, tour and travel, hotel expenditure or boarding and lodging expenses etc. are not be included in the employee's income as perquisite. This perquisite is tax free in the hands of an employee.

20) Travelling expenses paid or reimbursed

Actual travelling expenses paid or reimbursed by the employer for journeys undertaken by employees' business purpose are exempt.

21) Interest free loan

Any loan provided by the employer to an employee either free of interest or at concessional rate of interest, is tax free perquisite, if the amount of loan does not exceed Rs. 20,000.

6.6 DEDUCTIONS FROM 'SALARIES'

The income chargeable under the head 'Salaries' is subject to certain deductions allowable under section 16. They are:

i) Standard Deduction – Section 16(i)

ii) Entertainment Allowance – Section 16(ii)

iii) Tax on Employment – Section 16(iii)

Let us now discuss these deductions.

6.6.1 Standard Deduction [Section 16(i)]

This deduction is now again allowed W.e.f. assessment year 2019-20. The least of the following two amounts shall be deducted from gross salary of the employee:

a) Rs 50,000

b) Actual amount of gross salary

6.6.2 Entertainment Allowance [Section 16(ii)]

Entertainment allowance is normally given to Senior Officer. An employer gives allowances to his employee to spend it on the reception of the customers.

An entertainment allowance is part of salary. Hence, it is first to be included in the salary income. Thereafter, a deduction on Entertainment allowance which is given to both types of employee, government and non-government employee as explained below, will be allowed.

i) **Government employee:** The least of the following will be allowed as a deduction:

   a) Rs. 5,000, or

   b) 1/5th or 20% of the employee's salary, or

   c) Amount of entertainment allowance granted during the year.

   Meaning of Salary: For the purpose of entertainment allowance, only basic salary shall be considered. Any other allowance even dearness allowance (Inspite of being under terms of employment), fixed percentage of commission on turnover and dearness pay shall not be included in the salary for the purpose of deduction of entertainment allowance.

ii) **Non-government employee (including semi-Government employee, employees of statutory corporation and local authority):** From the assessment year 2002-03, the deduction of entertainment allowance to non-government employees has been abolished.

6.6.3 Tax on Employment [Section 16 (iii)]

This tax is also known as professional tax and it shall be deducted in the year in which it is actually paid. If any tax is realized on salary of the employee by the state government, this amount shall be deducted from the gross salary of the employee. As per the constitution of India, professional tax more than Rs 2,500 p.a cannot be levied upon the employee. If the professional tax is paid by the employer, it is first included in the salary income of the employee and after it is deducted from gross salary of the assessee, it is treated as general perquisite u/s 17(iv).

Illustration 10

Mr. Sanjay is employed in Reserve Bank of India as Manager. He gives the following details for the P.Y. 2020-21. Compute gross and taxable salary income for the A.Y. 2021-22.

i) Basic pay Rs. 48,000 p.m.

ii) Dearness allowances Rs. 18,000 p.m. (20% is used for benefits of retirement)

iii) House Rent Allowance (HRA) Rs. 15,000 p.m. He pays 18,000 p.m. as rent for his accommodation in Chennai

Solution:

Computation of Gross Salary of Mr Sanjay for AY 2020-21	Rs.
Basic salary (Rs. 48,000 × 12)	5, 76,000
D.A. (Rs. 18,000 ×12)	2, 16,000
H.R.A	25,920
Gross Salary	8, 17,920
Less: Standard deduction	50,000
Taxable Salary	**7, 67,920**
Calculation of H.R.A	
Least of the following amount will be exempt.	
i) Actual H.R.A. received (15,000×12)	1,80,000
ii) (Rent paid – 10% of salary) (2, 16,000– 61,920)	1, 54,080
Salary = (5, 76,000 + 43,200)	6, 19,200
iii) 50% of salary	3,09,600
Exempted amount	1, 54,080
Taxable amount = Rs. (1, 80,000 – 1, 54,080)	25,920
Note:	
1) Salary = 48,000 × 12= Rs 5,76,000	
2) DA= 2,16,000 × 20%= Rs 43,200	

Illustration 11

Mr. Rajeev an employee in a firm gets Rs 5,000 p.m. as salary, Rs. 800 p.m. as dearness allowance and Rs. 300 as city compensatory allowance. He is getting entertainment allowance of Rs. 800 p.m. He paid professional tax of Rs. 2,500. He is also getting a bonus equal to three month's salary. He resides in Agra (having population more than 25 lakhs) in a house owned by the firm. Fair rent of house is 1,500 p.m.

Compute his income under the head 'Salaries' for A.Y. 2021-22.

Solution:

Computation of Taxable Salaries of Mr Rajeev for AY 2021-22	Rs.
Salary @ Rs. 5,000 p.m	60,000
D.A. @ 800 p.m	9,600
C.C.A. @ 300 p.m	3,600
Entertainment allowance @ 800 p.m	9,600
Bonus equal to three month's salary	15,000

Perquisite:

Rent-free house @ 15% of salary 15% of 88,200 [60,000 (B.S) + 3,600 (C.C.A.) +9,600 (E.A.) + 15,000 (B)]	Rs. 13,230
Gross salary	1,11,030
Les: (i) Standard deduction	50,000
	61,030
Less: (ii) Professional tax	2,500
Taxable salary	**58,530**

Note:

i) D.A. is not included in salary for calculation of rent-free accommodation because it is not under the terms of employment.

ii) No deduction is allowed in respect of Entertainment allowance, as Mr. Rajeev is not a government employee.

Illustration 12

Mr. Radhey Shyam is employed in a company. He gets the following from the company:

i) Salary @ 20,000 p.m.

ii) Dearness allowance @ Rs. 2,000 p.m.

iii) Medical allowance @ Rs. 5,000 p.m.

iv) Bonus equal to 2 month's salary

v) Commission @ Rs. 20,000 p.a.

The following perquisites are provided by the employer:

i) A sweeper and a cook getting salary of Rs. 1,500 p.m. each.

ii) A car of 1400 cc for his personal use for which the employer pays.

iii) Rent-free unfurnished house in Etawah (Population less than 10 lakhs) owned by employer, annual rental value of which is Rs. 1,00,000

iv) A gardener whose salary is Rs. 2,000 p.m.

v) Free gas, electricity and water facility for private use, employer actually paid for this facility Rs. 20,000 for previous year.

Compute taxable salary of Mr. Radhey Shyam for the A.Y. 2021-22.

Solution:

Taxable salary of Mr. Radhey Shyam for the A.Y. 2021-22	Rs.
Salary @ Rs. 20,000 p.m	2, 40,000
D.A. @ Rs. 2,000 p.m	24,000
Medical allowance @ Rs. 5,000 p.m	60,000
Bonus equal to 2 months' salary	40,000
Commission	20,000
Rent free house (7.5% of salary)	26,250

Sweeper and Cook	Nil	
Car	Nil	
Free gas, electricity and water	Nil	
Gross salary		4, 10,250
Less: Standard deduction	50,000	
Taxable Salary		**3, 60,250**

Note:

1) Valuation of rent-free house 7.5% of 3,50,000 = Rs, 26,250 [Salary = Rs. 2,40,000 (B.S) + Rs. 50,000 (Medical Allowance.) + Rs. 40,000 (Bonus) + Rs. 20,000 (Commission) = 3,50,000]

2) Mr. Radhey Shyam is not a specific employee, so perquisite of sweeper, cook, gas, electricity, water and car is not taxable.

3) Facility of gardener is not regarded as perquisite because it is provided with a house owned by the employer.

4) Standard deduction can be allowed maximum up to gross salary.

Check Your Progress B

1) State whether following statements are True or False:

   i) In respect of Government employees, ten percent of cost of furniture should not be added while computing the perquisite value of the furnished house.

   ii) For computing the value of rent-free accommodation 'salary' for the entire year should be considered irrespective of the period of occupation of the house.

   iii) Facility of telephone provided to a specified employee is taxable perquisite.

   iv) If the house is not owned by the employer, salary of gardener and maintenance expenses of the garden should not be added.

   v) Free gas, supplied by Indian Oil Corporation to its employees is a taxable perquisite.

   vi) Value of subsidized lunches is exempt while the value of free lunches is taxable perquisite.

   vii) When car is owned by employer and all the expenses are borne by employee if car is used only for official use, the values of perquisite will be Nil.

   viii) Any gift or token received from employer shall be exempted upto Rs. 10,000.

   ix) Mr. Sahil went to Shimla. He stayed there in guest house of the company and saved Rs. 5,000 on account of accommodation. It is taxable.

   x) Advance salary is not taxable under the head 'Salaries'.

2) What are the provisions relating to Leave Travel Concession as per Income Tax Act, 1961?

....

....

....

3) What do you understand by Deductions? Explain.

....

....

....

6.7 LET US SUM UP

Apart from cash payment, an employee also receives certain benefits in kind which can be convert into cash. These are called Perquisites. There are three types of Perquisite; it may be tax-free, taxable for specified employees, taxable for all employees. These Perquisites are to be valued and included in the salary of an employee. After the value of Perquisites is calculated and included in the salaried income, certain deductions are available from the gross salary. They are:

i) Standard deduction

ii) Entertainment allowance

iii) Tax on employment

The net taxable income under the head salary is arrived at after deducting the quantum of permissible deductions mentioned above, from the gross income from salaries.

6.8 KEY WORDS

Accommodation: This refers to the residential house provided to the employee by the employer either free of rent or at concessional rent.

Monetary income: This represents receipts obtained by a salaried employee by way of money. Obviously, perquisite in kind is to be excluded while calculating monetary income.

Perquisite: Casual emolument, Payment, fee or profit attached to an office.

Personal accident policy: This is policy usually taken on the life of certain key executives whose functions and movement may expose then to fatal accidents or whose existence is for the company's prosperity. The premiums are invariably paid by the employer.

Specified Employee: The term denote those employees who are directors, employees substantially interested in a company or when monetary income under the head 'salaries' exceeds Rs. 50,000.

6.9 ANSWERS TO CHECK YOUR PROGRESS

Check Your Progress A

1) Salaries
2) Employer
3) Tax free
4) 10%
5) 15

Check Your Progress B

i) False, ii) False, iii) False, iv) True, v) False, vi) False, vii) True, viii) False, ix) True x) False

6.10 TERMINAL QUESTIONS / EXERCISES

1) What is not included in 'Salary' for calculating the value of rent-free accommodation for a public employee?

2) What are the provisions of section 16 (ii) regarding entertainment allowance for non-government employees?

3) Compute the monetary income of 'A' from the following particular for A.Y. 2021-22 to ascertain whether he is a specified employee or not. Rs.

a)	Basic salary	18,000 p.m.
b)	D.A. (not forming part of salary for calculating retirement benefits)	5,000 p.m.
c)	Education allowance	2,000 p.m.
d)	Income tax paid by the employer on behalf of A.	1,000 p.m.

[Answer: A is a specified employee as his monetary income is more than Rs. 50,000 i.e. Rs. 38,000]

4) Mr. Sanjay is a private sector employee. He received the following emoluments. Rs.

a)	Basic pay	8,000 p.m.
b)	D.A. (not included for computing retirement benefits)	800 p.m.
c)	Bonus (for the year)	15,000
d)	H.R.A. received	9,000 p.a.
e)	Exempted H.R.A.	5,000
f)	Education allowance (He has two children)	500 p.m.

Compute 'salary' for the purpose of arriving at the perquisite value for rent-free accommodation.

[Answer: Rs. 1, 18,600]

5) Mr. Rakesh is employed in MNC. He received the following from the company. Rs.

a)	Salary	20,000 p.m.
b)	D.A.	2,000 p.m.
c)	Medical allowance	5,000 p.m.
d)	Bonus equal to 2 months basic salary.	
e)	Commission	20,000 p.a

The following perquisites are also provided by the employer.

i) Rent-free unfurnished accommodation at Agra owned by employer.

ii) Sweeper and a Cook getting salary of Rs. 1,500 p.m. each.

iii) A Gardner getting salary of Rs. 2,000 p.m.

iv) Free gas, electricity and water facility for personal use for which the employer pays Rs. 20,000 during the P.Y.

Compute taxable salary of Mr Rakesh for the A.Y. 2021-22

[Answer: 4,68,000]

6) Mr. Sahay joined Surya Private Ltd. His basic salary is Rs. 40,000 p.m. D.A. Rs. 2,000 p.m, education allowance Rs. 500 for one child and Rs. 1,500 p.m. as entertainment allowance during the P.Y. 2020-21. He paid Rs. 10,000 as professional tax. Determine his taxable salary for the A.Y. 2021-22.

[Answer: 4,66,800]

7) Mr. Rashid is employed in Khadi Gramodyog in Kanpur on a monthly salary of Rs. 12,000 p.m. He is getting bonus as two months' salary, entertainment allowance Rs. 5,000 p.a. The employer provides following perquisites.

a) Car of 1800 c.c. for both private and official use. All the expenses are borne by the employer.

b) He has been given a personal loan of Rs. 50,000 at 5% interest on 1st Jan., 2020.

c) The employer spent Rs. 10,000 on the education of his son who is abroad.

d) The employee paid Rs. 4,000 as professional tax for the P.Y. 2020-21

Compute taxable income from salary of Mr. Rashid for A.Y. 2021-22

(Note: Assume rate of interest for personal loan is 11.9% as given by State Bank of India)

[Answer: 1,58,663]

8) Mr Riyaz is reader in a college, run by a society, on a monthly salary of Rs 50,000. Besides salary he also gets 45% of salary as dearness allowance, Rs 1000 p.m., entertainment allowance and Rs 1000 p.m. as proctor's allowance. During the year, he gets Rs 500 p.m. as additional DA. Arrears of salary received Rs 30,000.

He contributes 10% of his salary to provident fund. The college contributes an equal amount interest credited to his provident fund @12% amounted to Rs 40,000.Three children of Mr Riyaz are studying in an institution run by the society , which runs the college for which to Rs 1,500 p.m. for one student. Mr Riyaz is provided with a rent free accommodation in a city (population 13 lakhs) which is owned by the college. Its fair rental value is Rs 2,500 p.m. A Gardner for the upkeep of the garden on the back side of the house is also provided. The salary of Gardner amounting to Rs 300 p.m. is also paid by the college. During the year Mr Riyaz proceeded on two months leave with full pay to his home at Jaipur. The college paid Rs 6,500 being the air fare to and from Jaipur for him and his wife for this purpose.

Compute the taxable salaries income of Mr Riyaz for the year ending on 31st march, 2021, for the assessment year 2021-22.

[Answer: Taxable salary = Rs. 9,68,733]

Note: These questions will help you to understand the unit better. Try to write answer for them. But do not submit your answers to the University. These are for your practice.

UNIT 7 SALARIES-III

Structure

7.0 OBJECTIVES

After studying this unit, you should be able to:

- list different types of provident funds and their treatment for tax purposes;
- enumerate and calculate the amount of deductions available u/s 80C; and
- compute the taxable income from salary after taking into account the provident fund and deduction u/s 80C.

7.1 INTRODUCTION

In units 5 and 6, we have learnt about the items included in the salaried income of an employee. Apart from many allowances and perquisites, there are some other benefits available to a salaried employee; provident fund is one of such benefits. In the unit, we will study in detail the provident fund schemes, different kinds of provident fund and their tax-treatments. We will also study the various deductions available to a salaried individual u/s 80C in respect of savings.

7.2 PROVIDENT FUND SCHEMES

Provident means to provide for future. Provident fund is a fund which is created to help an individual in future, i.e., after retirement or death. The employee contributes certain amount every month out of his salary and an equal amount is contributed by the employer. This amount is invested in government securities and earns a certain amount of interest. The interest so earned on the balance standing in the account of the employee is credited to his provident fund account. This amount gets accumulated over a period of time. The whole amount accumulated over years is given to the employee at the time of retirement or voluntary retirement and is paid to the legal heir after the death of the employee. There are different kinds of provident funds. The employee can deposit the amount in any of the provident fund. The different kinds of provident funds are:

i) Statutory-Provident Fund

ii) Recognized Provident Fund

iii) Unrecognized Provident Fund

iv) Public Provident Fund

v) Approved Superannuation Fund

Let us now discuss them one by one.

7.2.1 Statutory Provident Fund

Statutory provident fund is set up under Provident Fund Act, 1925 and is maintained by Government and Semi-government department, Reserve Bank of India, State Bank of India, Railways, Statutory corporations, Universities, colleges and local bodies etc.

7.2.2 Recognized Provident Fund

This is a provident fund which is recognized by the commissioner of Income Tax in accordance with the rules contained in part A of the Fourth Schedule of the Income Tax Act, 1961. It includes a provident fund established under a scheme framed under the Employees Provident Fund Act, 1952. It must be remembered that it is important for tax purpose. For example, where a provident fund is recognized by the provident fund commissioner but not by the commissioner of Income Tax, then the tax concessions under the Income Tax Act cannot be extended to the contributions to such provident fund.

7.2.3 Unrecognized Provident Fund

This is a provident fund which is not recognized by the Commissioner of Income Tax. Since it is not recognized, no relief is granted to the assessee for tax purpose. In other words, it can neither be termed as statutory provident fund nor a recognized provident fund. Such a fund is normally maintained by private employers.

7.2.4 Public Provident Fund (PPF)

Regular salaried employees save money in provident fund through deductions from their salaries. For the benefit of the public, particularly for self-employed person such as doctors, lawyers, accountants, actors, traders, the central government introduced the PPF scheme. PPF scheme was started from 01/07/1968. Its main aim is to encourage savings. Individuals and association of persons can deposit in the public provident fund accounts, as and when their resources permit. Even salaried employees can save through PPF in additions to their regular provident funds. PPF accounts can be opened at any branch of the State Bank of India or its subsidiaries or at any head post office and specified branches of nationalized banks. Any individual can subscribe to PPF any amount not less than Rs. 500 and not more than Rs. 1, 50,000 in a year. Interest is credited at the end of each year, but is payable only at the time of maturity. The accumulated sum in PPF account is payable after 15 years and after completion of 15 years, the whole amount together with interest is exempt from income tax. An assessee can extend this account further for period of 5 years. Non-resident Indians and HUF are not eligible to open this account.

7.2.5 Approved Superannuation Fund

This means a superannuation fund approved by the Commissioner of Income Tax accordance with the rules contained in part B of the Fourth Schedule of the Income Tax Act. It is significant to note that the sole purpose of the above fund should be the provision of annuities for employees on their retirement after a specified age of on their becoming incapacitated prior to such retirement or for the widows or dependence of such employees on their death.

7.3 TAX TREATMENT OF PROVIDENT FUND

You studied the different kinds of provident funds in this unit point 7.2. Let us now study various provisions of Income Tax Act, 1961 with regard to these funds. Tax exemptions in relation to this fund are as under:

i) Employer's contribution is exempt from tax

ii) Employee's contribution qualifies for deduction under section 80C

iii) Interest on accumulated balance is exempt from tax

Table 7.1 will help you to understand the provisions of provident fund relating to the above.

Table 7.1: Provisions of Provident Funds

Particulars	Statutory P.F.	Recognized P.F.	Unrecognized P.F	Public P.F
Employee's / assessee's contribution	Employee is paid his monthly salary after deducting his contribution to provident fund but Employee's contribution in SPF is included in taxable salary. But the entire contribution qualifies for deduction u/s 80C.	Employee is paid his monthly salary after deducting his contribution to provident fund but Employee's contribution in RPF is included in taxable salary. But the entire contribution qualifies for deduction u/s 80C.	Employee is paid his monthly salary after deducting his contribution to provident fund but Employee's contribution in URPF is included in taxable salary. But the entire contribution does not qualify for deduction u/s 80C.	Deduction u/s 80C is available from gross total income subject to the limited specified amount.
Employer's contribution	Exempt	Tax free upto 12% of salary. Excess over 12% of salary is included in salary.	Exempt	The employer does not contribute

Interest credited to provident fund	Exempt	Tax free (u/s 10) upto 9.5% p.a rate of interest; excess over 9.5% is included in gross salary	Exempt	Exempt
Lump-sum payment at the time of retirement or termination of service etc.	Exempt u/s 10 (11)	Tax free u/s 10 (12) provided: (i) the employee has served continuously for at least 5 years, or (ii) he has been removed from service on account of retrenchment, illness or closure of business.	Lump sum upto the amount equal to employee's contribution and interest thereon is included in salary income. Interest on employee's contribution is taxable under the head. 'Income from other sources'.	Exempt

Illustration 1

Mr. Gaurav Modi is employed in Khadi Samiti in Lucknow. He is in receipt of a salary of Rs. 17,000 p.m. and a dearness allowance of Rs. 2,000 p.m. He contributes 10% of his salary and dearness allowance to a provident fund to which Khadi Samiti contributes 15%. He is provided with a rent free unfurnished house by his employer. He received Rs. 25,000 as bonus during previous year. The interest credited to his provident fund @ 12% amounted to Rs. 1,000.

Compute taxable income of Mr. Gaurav Modi for the assessment year 2021-22, if the P.F. in question is (i) Statutory (ii) Recognized or (iii) Unrecognized. On what amount the assessee is entitled to deduction u/s 80C.

Computation of Taxable Income of Mr. Gaurav Modi for AY 2020-21

	Statutory P.F. P.F. (Rs.)	Recognized P.F. (Rs.)	Unrecognized P.F. (Rs.)
Salary @ 17,000 p.m.	2,04,000	2,04,000	2,04,000
D.A. @ 2,000 p.m.	24,000	24,000	24,000
Bonus	25,000	25,000	25,000
Employer's contribution to R.P.F. in excess of 12%	—	6,840	—
Interest credited to R.P.F.in excess of 9.5%	—	208	—
Value of rent free house 10% of salary of Rs. 2,53,000 (as population of Lucknow exceeds 10 lakhs but does not exceed 25 lakhs)	25,300	25,300	25,300
Gross Salary	2,78,300	2,85,348	2,78,300
Less: Standard Deduction	50,000	50,000	50,000
Taxable Salary	2,28,300	2,35,348	2,28,300
Amount entitled to deduction u/s 80C	22,800	22,800	Nil

Note: Calculation of Recognized P.F.

1) Employer's contribution RPF = 2, 28,000 (Salary + D.A.)

$$= 2,28{,}000 \times \frac{3}{100} = 6{,}840$$

Interest credited $= \dfrac{1000 \times 100}{12} = 8333.33$

Excess of 9.5% $= \dfrac{8{,}333 \times 2.5}{100} = 208$

2) Assessee is entitled to deduction u/s 80C, upto a maximum amount of Rs. 1,50,000 in respect of his contribution to statutory or recognized provident fund, i.e. 10% of his salary and D.A., say Rs. 22,800. He is not entitled to deduction u/s 80C in respect of his contribution to unrecognized provident fund.

3) Salary = Basic Pay + D.A+ Bonus

= 2,04,000+ 24,000+25,000 = Rs. 2,53,000

7.4 CERTAIN OTHER ASPECTS OF TAXABLE SALARY

While calculating the taxable income from salary, we should take into account the following aspects of salary:

1) **Waivers of salary**: Once salary accrues to an employee, it becomes taxable under Section 15. Even if the employee waives his right to receive payment thereof it will be considered as a mere application of his income and his tax liability will not be affected.

2) **Surrender of salary**: However, if any employee surrenders his salary to the central government under Section 2 of the Voluntary Surrender of Salaries, then the salary so surrendered will be excluded while computing his salary income.

3) **Tax-free salaries**: An employer can choose to pay the tax on behalf of the employee and refrain from deducting the same from the salary paid to the employee. However, while computing the income of the employee, the tax so paid by the employer will be added to the salary income of the employee.

7.5 DEDUCTION UNDER SECTION 80C

Section 80C allows certain investments and expenditure to be tax-exempt. Under this section, deduction is allowed in respect of specified qualifying amount paid or deposited by individual or H.U.F taxpayer (assessee) only.

7.5.1 Gross Qualifying Amount

Deductions in respects of contribution to life insurance premium, Deferred Annuity, Provident Fund and Public Provident Fund and subscription to certain shares and debentures, etc. (Sec. 80C). This deduction is available on the basis of specified qualifying investments/contributions/ deposits/payments (Gross Qualifying Amount) made by the taxpayer during the previous year.

Eligibility of Assessee: This deduction is allowed only to the following assesses from their gross total income computed as per the provisions of the Act:

i) An individual or

ii) A Hindu Undivided family

Deduction on account of the following saving/investment cannot exceed Rs. 1,50,000. The above assesses shall be entitled to a deduction of whole of the amount paid or deposited in the previous year, being the aggregate of sum referred to below as does not exceed Rs. 1,50,000.

A) In case of Individual Assessee

i) Life Insurance Premium: The premium paid by an assessee on his own life, on the life of spouse (husband or wife) and children, contribution of employee in insurance plan, joint life premium and group insurance W.e.f. Assessment Year 2019-20 maximum 20% of sum assured shall be allowed as deduction u/s 80C.

a) Insurance policy may be taken by the assessee for his desired amount but only 20% of insurance amount or actual premium paid (whichever is less), shall be included in total limit for deduction u/s 80C. (If policy is taken before 01.04.2012 and 10% if policy is taken after 31.03.2012)

b) No deduction u/s 80C will be allowed on the amount of premium paid on insurance policy taken by the assessee on the life of his/ her parents.

c) Life Insurance Corporation may issue various types of insurance policies, e.g. whole his insurance policy, Bima Gold, Endowment Insurance Policy, Jeewan Mitra Policy, etc. The assessee may take any one or more insurance plan.

d) The children, who have been insured, may be married, unmarried dependent or independent upon the assessee.

ii) Deferred Annuity: To effect and to keep in force a contract for a deferred annuity on the life of spouse and children.

iii) Contribution of employee in Statutory Provident Fund.

iv) Contribution of employee in Recognized Provident Fund.

v) Contribution in Public Provident Fund upto maximum Rs. 1,50,000.

vi) Payment under Unit Linked Insurance Plan, 1971.

vii) Amount deducted out of salary of Government employee or deferred annuity or for provision to wife and children restricted to $1/5^{th}$ of salary.

viii) Contribution in Approved Superannuation Fund.

ix) Contribution in Notified Central Government Securities or in Notified Deposit Scheme. For this section, investment in 6 years National Saving Certificate VIII or IX issue and deposits in National Saving Scheme, 1992 have been recognized.

x) Re-investment of accrued interest on National Saving Certificate (NSC) VIII.

xi) Deposit in National Housing Scheme or contribution in pension fund, e.g. Housing Loan Scheme.

xii) Contribution in the following deposit schemes:

a) A public sector company, which provides long-term loans for the purchase or construction of residential house, or

b) Any authority established in India through and Act for solving the housing problems or formed for development of cities, towns or village or for both the purpose.

xiii) Refund of loan (Principal amount only) taken for the construction of house. Following points are essential to be considered in this refund of loan.

a) Payment of any installment or its part under scheme of construction and sale of the house by any self-financing or development authority, housing board or other authority.

b) Payment of any installment or its part to any company or co-operative society of which the assessee is member for allotment of the house.

xiv) Contribution in Mutual Fund establishment u/s 10(23D) or in units of Equity Linked Saving Scheme of Unit Trust of India.

xv) Contribution in pension fund notified u/s 10(23D) in mutual fund established by Unit Trust of India.

xvi) Tuition fee for children education: Tuition fee paid by assessee for his children education shall be allowed as deduction u/s 80C provided following condition are satisfied:

a) It should be paid for school, college, university within India;

b) The fee should be paid for full time education;

c) It should be paid in connection with maximum 2 children; and

d) Tuition fee does not include college development fee, sports, library fee, donation etc.

xvii) Any sum paid or deposited in name of girl child under the Sukanya Samridhi account scheme W.e.f AY 2015-16.

xviii) Payment made by an individual for notified annuity plan of the life insurance corporation or any other insurer. New jeevan dhara, New jeevan dhara-I and New jeevan Akshay, New jeevan Akshay-I and New jeevan Akshay-II are notified schemes.

B) In case of a Hindu Undivided Family

A Hindu Undivided Family may make following payments in previous year:

1) Amount of premium on the life insurance of any member of family. Premium to be included in deductible amount for deduction shall be restricted to 20% of sum assured. (if policy is taken before 01.04.2012 and 10% if policy is taken after 31.03.2012)

2) Contribution in Public Provident Fund in the name of any member of the family

3) Contribution in Notified Central Government Securities or Notified Deposit Scheme. It includes 6 year National Saving Certificates VII Issue and National Saving Scheme, 1992.

4) Contribution in Mutual Fund established u/s 10(23D).

5) National Saving Certificate, VII Issue.

6) Accrued interest on NSC VIII Issue.

7) Deferred Annuity, Annuity paid by an assessee on self, on spouse, children or under deferred annuity agreement.

8) Contribution in any deposit scheme of the following:

   a) Company of Public Sector, which provides long-term loans for the purchase and construction of residential houses, or

   b) Any authority established in India under any Act, whose formation was made for solving the residential problem or for the betterment and improvement of cities, village or towns or for both the purposes.

9) Amount paid on the purchase or construction of New Residential House. Any amount paid for the purpose of purchase or construction of a residential house property, the income of which is taxable under head 'Income from House Property'. Such payment may be made by way of:

   a) An installment or part payment of the amount due under any self-financing or other scheme of any development authority, housing board or other authority engaged in the construction and sale of house property; or

   b) Payment of any installment or its part to any company or co-operative society of which the assessee is a member for allotment of the house.

   c) Repayment of borrowed money by the assessee taken from the following.

      i) Central or State Government, or

      ii) Bank (including co-operative bank)

      iii) Life Insurance Corporation, or

      iv) National Housing Bank or

v) Such public company whose main object is to provide long-term finance for purchase/construction of houses for residential purposes.

vi) Assessee's employer, if such employer is in the form of an authority or a board or a corporation or any other body established under a Central or State Act.

d) Stamp duty, registration fee and other expenses for the purpose of transfer of such house to possess ownership (But expenses of repair and renew shall not be included).

10) Contribution in National Housing Bank Deposit Scheme or contribution in any pension fund established by it, e.g. Housing Loan Scheme.

11) Contribution in Mutual Fund established u/s 10(23D) or in units of Equity Linked Saving Scheme or Unit Trust of India.

12) Investment in Term Deposit:

a) Investment in scheduled bank for not less than 5 years.

b) Such investment must be in accordance with a scheme framed and notified by the Central Government in the official Gazette.

13) Any sum paid or deposited in name of girl child under the Sukanya Samridhi account scheme W.e.f AY 2015-16.

14) Payment made by an HUF for notified annuity plan of the life insurance corporation or any other insurer. New jeevan dhara, New jeevan dhara-I and New jeevan Akshay, New jeevan Akshay-I and New jeevan Akshay-II are notified schemes.

Note:

i) Investment/Deposits are qualified on payment basis u/s 80 C, the amount paid are eligible for rebate. Thus, the payment made in previous year is eligible for deduction, whether such payments are related to last year or next year. Hence, if the payment is due but outstanding, no deduction will be admissible on it.

ii) If Joint Life Premium is paid by the assessee on the joint life of self or spouse or children, the deduction on payment of premium is admissible, but if joint life policy is with other outsiders, no such deduction will be allowed.

Interest Table accrued on N.S.C. (VIII Issue)
Interest accruing on a certificate of Rs. 100

The year for which interest accrued	01/03/03 To 30/11/11	01/12/11 To 31/03/12	01/04/12 To 31/03/13	01/04/2013 To 31/03/2016
Rate %	08.00	-	8.60	8.50
First year	08.16	8.58	8.78	8.68
Second year	08.83	9.31	9.56	9.43
Third year	09.55	10.11	10.40	10.25
Fourth year	10.33	10.98	11.31	11.24
Fifth year	11.17	11.92	12.30	12.11
Sixth year	12.08	NA	NA	NA

Interest accruing on a certificate of Rs. 100

	01/04/2016 to 30/09/2016	01/10/2016 to 31/03/2017	01/04/2017 to 31/06/2017	01/07/2017 to 31/12/2017	01/01/2018 to 31/03/2019
First year	8.10	8.00	7.90	7.80	7.60
Second year	8.76	8.64	8.52	8.41	8.18
Third year	9.46	9.33	9.20	9.06	8.80
Fourth year	10.23	10.08	9.92	9.77	9.47
Fifth year	11.06	10.88	10.71	10.53	10.19

NSC IX ISSUE

The table shows the amount of interest accrued at the end of each year:

	Interest accruing on a certificate of Rs. 100 when investment is made		
Year for which interest accrues	**W.e.f 01/12/2011 To 31/03/2012**	**04/01/2012 To 31/03/2013**	**On or after 04/01/2013**
1st year	8.89	9.10	8.99
2nd year	9.68	9.93	9.80
3rd year	10.54	10.83	10.68
4th year	11.48	11.81	11.64
5th year	12.50	12.89	12.69
6th year	13.61	14.06	13.83
7th year	14.82	15.34	15.08
8th year	16.13	16.74	16.43
9th year	17.57	18.26	17.91
10th year	19.13	19.92	19.52

Important Note: National Saving Certificates VIII become mature after 6 years accrued interest of 6th year is not treated re-invested. Hence, no deduction u/s 80C on this interest of 6th year is allowed.

Cancellation of deduction under Section 80 C: Under the following circumstance, the deduction shall be cancelled:

1) If after paying two years premium, the life policy is terminated on notice or the policy is terminated on account of non-payment of premium, the premium of that year will not be eligible for deduction u/s 80C and whatever deduction has been availed under this section earlier, such amount shall be added in the income of the assessee.

2) If this contribution is stopped before 5 years, the deduction will not be allowed in the year of closing. The deduction allowed in earlier year on such contribution shall be included in income in the year of its closing.

3) If an assessee has got deduction under section 80 C in connection with loan taken for purchase or construction of residential house and he sells that house within 5 years , the deduction already availed shall be cancelled .This cancelled deduction shall be included in taxable income of the years in which it is cancelled .

4) If an assessee has got deduction u/s 80 C by purchasing shares or debentures of an infrastructure company and he sells them within 3 years after date of purchase, the deduction already availed will be cancelled and such deduction shall be included in the income of the year in which it is cancelled.

Check Your Progress A

1) A person who is a Government employee saves the following amount.

   a) Rs. 2,000 as premium on LIC

   b) Rs. 3,000 as contribution to Statutory Provident fund.

   c) Rs. 4,000 in ULIP

   d) Rs. 12,000 as repayment of loan taken for the house

   e) Rs. 4,000 in Jeevan Mitra

   Calculate the Gross qualifying amount.

2) Fill in the blanks:

   a) Interest credited to a Statutory Provident Fund is ………… in the salary income.

   b) A person can deposit Rs. 500 to ………… in year in PPF.

   c) Contribution to Jeevan Dhara and Jeevan Akshay are entitled for deduction u/s……………..

Computation of Taxable Salaries

Specimen of computation of taxable salaries of Mr………

For the assessment year……….

Salary @ Rs ……………p.m.	…………
Annuity of Pension	…………
Bonus, Fees, Commission etc	…………
Dearness Allowance or Dearness Pay	…………
Taxable salary of Gratuity	…………
Taxable part of encashment of earned leave	
Allowances	
Entertainment allowance	…………
Education allowance (Taxable portion)	…………
Any other taxable cash allowance	…………
House rent allowance (taxable portion)	…………
Special allowance (Actual- spent for employment purpose)	…………

Travelling allowance (Actual amount spent for business purpose)	…………
Employer's contribution to RPF in excess of 12% of salary	…………
Interest credited to RPF in excess of 9.5% rate	…………
Perquisites	
Valuation of rent free/concessional rent free accommodation	…………
Actual payment of employee's obligation paid by the employer	…………
Life or annuity premium paid by employer	…………
Valuation of perquisites, if any, to specific assessee	
Director or employee having substantial interest or having monetary salaries income in excess of Rs 50,000, if the assessee is not a specific assessee, these perquisites shall not be valued as these perquisites shall be deemed free or exempt	
Profit in Lieu of salary	
Compensation for modification in terms of or termination of services	…………
Taxable portion in transferred balance of unrecognized PF	…………
Gross Salaries	…………
Less: i. Standard Deduction	…………
ii. Entertainment Allowance	…………
iii. Professional or Employment Tax	…………
Taxable Salaries	…………

You have studied the provisions of Income Tax Act. Let us now take a few illustrations to clarify the treatment of various contributions for tax purpose.

Illustration 2

Following particulars are furnished by Mr. Murari, a citizen and resident of India. Compute the taxable income of Mr. Murari for Assessment Year 2021-22

			Rs.
a)	Basic Salary		86,000
b)	House rent allowance (the house is at Kolar and Rent paid amount to Rs. 60,000)	42,000	
c)	LIC premium on his own life	5,000	
d)	Unit linked insurance plan contribution	1,000	
e)	Premium on his wife's life	2,500	
f)	Deposit in 10 years CTD of Post Office	2,000	
	Computation of Taxable income of Mr. Murari		

Solution:

Taxable salary of Mr Murari for AY 2021-22

	Rs.	Rs.
1) Basic Salary		86,000
2) House rent allowance:		
a) Actual HRA received	42,000	
b) Rent paid in excess of 10% of salary Rs. 60,000 – Rs. 8,600	51,400	
c) 40% of salary	34,400	
Taxable HRA (Rs. 42,000 – 34,400)		7,600
Gross Salary		93,600
Less: Standard deduction		50,000
		43,600
Deduction u/s 80 C		
Premium on own life	5,000	
Premium on wife's life	2,500	
Payment under unit linked plan	1,000	8,500
Taxable Income		**35,100**

Illustration 3

The following particulars are given by Mr. S. Rajan, Chennai, in respect of his annual income for the year ended 31.03.2021. Calculate taxable salary:

i) Salary (p.a.)	Rs. 1,70,000
ii) HRA	20% of salary
iii) Actual house rent paid	Rs. 1,200 p.m.
iv) Contribution to recognized provident fund	Rs. 20,000
v) LIP on his own life (sum assured Rs. 20,000)	Rs. 6,000
vi) Amount deposited in PPP account	Rs. 15,000

Solution:

Computation of income tax of Mr. S. Rajan for AY 2020-21

	Rs.	Rs.
Salary		1,70,000
House rent allowance		
i) Actual HRA received	34,000	
ii) Rent paid in excess of 10% of salary (17,000-14,400)	2,600	
iii) 50% of salary	85,000	
Taxable HRA (34,000 – 2,600)		31,400
Gross salary		2,01,400

Less: Standard Deduction	50,000	
Taxable Salary		**1,51,400**
Less – Deduction u/s 80 C		
LIP on his own life	6,000	
(Max 20% of sum assured)		
Contribution to RPF	20,000	
Contribution to PPF	15,000	41,000
Taxable Income		**1,10,400**

Illustration 4

Mr. Anurag is in a government service. His basic salary is Rs. 50,000 p.m. and getting dearness allowance @ 63% of the basic salary (it comes under the terms of employment). He contributes 10% of his salary in notified pension scheme. The central government contributes the same amount. He contributes Rs. 60,000 to public provident fund and paid Rs. 25,000 as premium on his life policy. Compute the taxable income of Mr. Anurag for the A.Y. 2021-22

Solution:

Computation of income tax of Mr. Anurag for AY 2021-22

	Rs,	Rs.
Basic salary @ 50,000 p.m.		6,00,000
Dearness allowance		3,78,000
Contribution towards pension scheme 10% on 9,78,000		97,800
Gross Salary		10,75,800
Less: Standard deduction		50,000
Net Salary		**10,25,800**
Less: Deduction u/s 80 C		
U/s 80 C for LIP & PPF (Rs. 25,000 + Rs. 60,000)	85,000	
U/s 80 CCD (1) contribution on to NPS	47,800	
(Being the amount contributed – Deduction allowed U/s 80 CCD (1B) i.e. 97,800 – 50,000 not exceeding 10% of salary)	1,32,800	
	1,32,800	
(Amount u/s 80 C, 80 CCC and 80 CCD (1) is limited to Rs. 1,50,000 hence u/s 80 CCD (1B) Amount Deposited in NPS [10% of salary or Rs. 50,000 (whichever is less) i.e. Rs. 97,800 of Rs. 50,000)	50,000	
U/s 80CCD (2) for employer's contribution to NPS upto 10% of salary of Mr. Anurag	97,800	2,80,600
Taxable Income		**7,45,200**

Illustration 5

Gross total income of Mrs. Neha is Rs. 6,75,000, she deposited in RPF Rs. 50,000. She paid donation to a Political Party Rs. 10,000 by cheque and Prime Minister National Relief Fund Rs. 15,000 by cheque. She paid medical insurance premia on the health of her spouse Rs. 27,000 by cheque. Compute her total taxable income for assessment year 2021-22.

Solution:

Computation of total taxable income of Mrs Neha for AY 2021-22

	Rs.	Rs.
Gross total income		6,75,000
Less: Deduction u/s 80 C RPF	50,000	
Deduction u/s 80 D		
Medical insurance premia		
(maximum deduction allowed Rs. 25,000)	25,000	
80G Donation to PMNRF	15,000	
Deduction u/s 80 GGC :		
Donation to political party	10,000	
		1,00,000
Rs. 6,75,000 – Rs. 1,00,000		
Taxable income		**5,75,000**

Illustration 6

An Indian citizen and not ordinarily resident Mr Rahul is an employee of an Indian company. He served in India for 4 months during the previous ended 31st march, 2021. For the balance of 8 months of the year he served in Singapore branch of the company. The particulars relevant to his assessment of this year were as under:

a) Salary @ Rs 15,000 per month for 4 months of service in India (April to July)

b) Salary @ Rs 20,000 per month for 8 months of service in Singapore (August to March)

c) Contribution to recognized provident fund @ 12% of salary for 4 months for service in India, the employer contributed at the same rate for the whole year.

d) Rahul was given free use of car of 1.4 liter cubic capacity, outside India; all expenses including those of a driver's salary were met by the employer.

e) Rahul was provided with rent free furnished accommodation throughout the period. The rent paid by the employer for the house was Rs 4,000 per month and Rs 4,500 per month in India and at Singapore respectively. The cost of furniture provided for Rahul's uses was Rs 15,000 at both places.

Compute Rahul's salary income for Assessment Year 2021-22.

Solution:

Computation of salary income of Mr Rahul for AY 2020-21

	Rs.	Rs.
Salary for 4 months @ Rs 15,000 p.m		60,000
Employer's contribution to RPF		
(12% of Rs 2,20,000	26,400	
Less: 12% of salary of Rs 60,000	7,200	19,200
Value of rent free furnished house in India	9,400	
Gross Salary		**88,6000**
Less: Deduction u/s 16		
Standard Deduction	50,000	
Income from Salary		**38,600**

Note:

1) Salary and allowance received in Singapore are not taxable as they have been earned and received in India, because Mr Rahul is not ordinary resident in India and he is not a government servant.

2) Salary for employer's contribution in PF :

4 months' salary in India (4×Rs 15,000)	Rs 60,000
8 month's salary in Singapore (8×Rs 20,000)	Rs 1,60,000
Total Salary for contribution	Rs 2,20,000

3) Valuation of house has been done as below:

15% of salary in India or rent paid by the employer in India	
Whichever is less (Rs 9,000 or Rs 16,000)	Rs 9,000
Add: 10% of cost of furniture (for 4 months)	
12,000×10% × 4/12	Rs 400

4) Employer's contribution in RPF is 12% of salary, but salary of 8 months accrued and received in Singapore shall not be taxable. Hence, whole amount of employer's contribution shall be treated for 4 months.12% of 4 month's salary in India shall be exempt. Remaining amount shall be taxable.

7.6 LET US SUM UP

Provident fund is an important fund in which a person contributes some amount and save income for future profit. Provident fund scheme applies in the most of the institutions. Under this, employer and employee both contribute some amount per month. At the time of retirement, the total amount of this fund along with the interest may be given to the employee.

Provident funds are five types:

i) Statutory Provident fund

ii) Recognized Provident fund

iii) Unrecognized Provident fund

iv) Public Provident fund

v) Approved Superannuation fund.

There are provisions in Income Tax Act, 1961 regarding the provident fund are related to the following:

i) Contribution of employee

ii) Contribution of employer

iii) Interest on balance

iv) Final payment

In Section 80 C, there are provisions regarding deductions related to saving from total income. Saving includes Life insurance premium, contribution in provident fund, contribution in ULIP, deposits in CTD, payment of residential housing loan, deposits in national banks, total of these savings are gross deductable amount. The amount of deduction may be calculated from gross deductable taxable amount for calculating taxable income. This amount is deducted from gross total income of the assessee.

7.7 KEY WORDS

Provident Fund: Fund created for future financial help to the person.

Statutory Provident Fund: This provident fund is maintained by Government or Semi-Government offices or bodies local authorities, railways, universities, colleges, banks, etc.

Recognized Provident Fund: This is recognized by the chief commissioner or the commissioner of Income tax.

Unrecognized Provident Fund: Provident fund which is maintained by private sector and not recognized by the chief commissioner or the commissioner of income tax.

Public Provident Fund: This is a fund which can be maintained by non salaried persons, any person salaried as well as self-employed can open this fund in S.B.I. and any nationalized bank.

Gross qualifying amount: Total saving amount which is deductible under Section 80C.

7.8 ANSWER TO CHECK YOUR PROGRESS

Check Your Progress A

1) Rs. 25,000

2) i) not included ii) Rs. 1, 50,000 iii) Sec 80 C

7.9 TERMINAL QUESTIONS/EXERCISES

1) What are the provisions regarding unrecognized provident fund in Income Tax Act, 1961.

2) Explain the rules for refund of loan taken for the construction of house.

3) Sri Suresh retired from Government service. During previous year he received the following. Rs.

1)	Salary from Government	2,00,000
2)	D.A. from Government	2,00,000
3)	Gratuity	10,00,000
4)	Commuted pension	12,00,000
5)	Encashment of earned leave	6,00,000
6)	Pension	4,32,000
7)	Provident fund	4,00,000

He contributed to LIC pension fund u/s 80 CCC Rs. 1,20,000 and deposited Rs. 60,000 in PPF. Compute his total income for the assessment year 2021-22.

[Answer: Rs. 6,32,000]

[**Note:** The incomes under point No. 3,4,5 and 7 in the above question is tax free]

4) Mr. Basu lives in Bhopal submit the following information in P.Y. 2020-21.

1)	Net salary after deduction on P.F. and deduction of tax at source	Rs. 2,40,000
2)	Income tax deducted at source on salary	8,000
3)	Employer's contribution to P.F.	12,000
4)	Employee contribution of P.F.	12,000
5)	Gross dividend from Indian company	8,000

Compute the taxable income of Mr. Basu for A.Y.2021-22

[Answer: Rs. 1,98,000]

[**Note:** Dividend from Indian company is exempt]

5) Mr Amit is employed in XYZ Ltd, getting basic pay Rs 15,000 p.m. and dearness allowance Rs 5,500 p.m. forming part of salary. He has contributed Rs 3,000 p.m. to the recognized provident fund and employer has also contributed an equal amount. During the year interest of Rs 25,000 was credited @ 8.5 % p.a

Employer has provided rent free accommodation to the employee for which rent paid by the employer is Rs 6,000 p.m. The employee has enchased one month leave and was allowed leave salary of Rs 17,000. Compute his income under the head salary for Assessment year 2021-22.

[Answer: Gross salary = Rs 3,13,970]

(**Hint:** Population of the city of accommodation is above 25 lakhs)

6) Mr. Jagdish is an employee of a company furnishes following particulars for previous year 2020-21

a)	Basic salary	1,2000 p.m.
b)	Dearness allowance (Not for retirement benefits)	1,200 p.m.
c)	Employee's contribution to RPF	10% of basic salary
d)	Employer's contribution to RPF	15% of basic salary
e)	Interest credited to P.F. on 31-10-2020	11% p.a. Rs. 5,500.
f)	Professional tax deducted to his salary Rs. 110 p.a. He has been provided with a rent free house for which he paid Rs. 1,000 p.m. The fair rent of the house is Rs. 8,000 p.a. He received Rs. 20,000 on 01-10-2020 for encashment of leave. Compute his taxable salary for A.Y. 2021-22 Assuming the population of city is 15 lakh.	

[Answer: Taxable salary = 1,36,550, Concessional Rent Rs. 4,400]

Note: These questions and illustrations are helpful to understand this unit. Do efforts for writing the answer of these questions but do not send your answer to university. It is only for yours practice.