TAXATION

Income tax

Income from "SALARY"

A Complete Revision

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INCOME FROM "SALARY"
A Complete Revision

Contents

1. Meaning

Salary means –

- Every payment,
- Made by employer to his employee,
- For the service rendered by him would be chargeable to tax.
- It includes both monetry payments (e.g. basic salay, bonus , commission, allowances etc.) as well as non-monetary facilities (e.g. housing accomodation, madical facility, interest free loan etc.)

Employer-Employee relationship – Relationship of employer and employee should be exist between payer and payee.

Examples:

a) Sujatha, an actress, is employed in Chopara Films, where she is paid monthly remuneration of ₹ 2 lakh. She acts in various films produced by various film producers. The for acting in such films is directly paid by Chopara Films by the different producers, in this case, ₹ 2 lakh will constitute salary in the hands of Sujatha, since the relationship of employer and employee exists between Chopara films and Sujatha.
b) In the above example, if sujatha acts in various films and gets fees from different producers, the same income will be chargable as income from profession since the relationship of employer and employee does not exist between Sujathaand film producers.
c) Commission received by a Director from a Company is salaryif the Director is an employee of the company.
d) Any salary, bonus, commission or remuneration by whatever name called due to or received by partner of a firm shall not be regarded as salary.

Full time or part-time employment: It does not matter whether the employee is full time employee or part-time employee.

Forgoing of Salary: Once salary accures, the subsequent waiver by the empoyee does not absolve him from liability of income-tax.

Surrender of Salary: If an employee surrenders his salary to the central government, the salary so surrender would be exempt from tax.

Salary paid tax-free: It means employer bears the burden of tax on the salary of the employee and income from salary in the hand of employee will consist the salary income and also the tax paid by the employer on this salary.

2. Definition of Salary

'Salary' under **section 17(1)**, includes the following

i. Wages,
ii. Any annuity or pension,
iii. Any gratuity,
iv. Any fees, commission, perquisite or profit in lieu of or in addition to any salary or wages,
v. Any advance of salary,
vi. Leave salary or leave encashment,
vii. Contribution to Recognised Provident Fund to the extand it is taxable,
viii. Transfer balance in Recognised Provident Fund to the extand it is taxable,

ix. Contribution made bu the government or other employer under a pension scheme reffered in section 80CCD.

3. Basis of charge

- Salary is chargable to tax either –

  'due' basis

  or

  'receipt' basis

  Whichever is **earlier**.
- Salary, paid in advance, is assessed in the year of payment, it cannot be susequently brought to tax in the year in which it becomes due.
- If the salary paid in arrears has already been assessed on due basis, the same cannot be taxed again when it is paid.

4. Palce of accural of salary

✓ **Section 9(1)(ii)**

Salary earned in india is deemed to accureor arise in india even if -

- It is paid outside India, **or**
- It is paid or payable after the contract of employment in India comes to an end.

  Example:

  If an employee gets pension paid abroad in respect of the services rendered in India, the same will be accure in India. Similarly, leave salary paid abroad in respect of the leaveearned in India is deemed to be accure or arise in India.

✓ **Section 9(1)(iii)**

Salary payable by the gavernment to a citizen of India for the services outside India shall be deemed to be accure or arise in India.

✓ **Section 10(7)** :

Any allowances or perquisite paid or allowed outside india by the government to citizen of india for rendering servicesoutside india will be fully **exempt**.

5. Profits in lieu of salary [Section 17(3)]

It includes the following :

i. Compensation due to or received by an employee from his employer or formar employer at or in connection with the termination of his employment.

ii. Compensation due to or received by an employee from his employer or formar employer at or in connection with the modification of the terms and condition of the employment.

iii. Any payment due to or received by an assessee from his employer or fromer employer from a provident or other fund, to the extant to which it does not consist of employee's contribution or interest on such contributions.

6. Advance Salary

Advance salary is taxable when it is received by the employee irrespective of the fact whether it is due or not.

7. Loan or Advance against salary

When an employee taken any loan from his employer, then such loan amount cannot be brought to tax as salary of the employee

Imp.- Adavnce against salary is different from advance salary. It is an advance taken by thr employee from his employer. This advance is generally adjusted with his salary over a specified time period. It cannot be taxed as salary.

8. Arrears of salary

It is charged on due basis.

9. Annuity

- Annuity is a sum payable in respect of a particular year.
- As per the defination of salary, 'annuity' is treated as salary.
- Annuity received from present employer is to be taxed as salary.
- Annuity received from past employer is taxable as profit in lieu of salary.
- Annuity received from a person other than employer is taxable as 'Income from Other Sources'.

10. Gratuity [Section 10(10)]

Gratuity is voluntary payment made by employer in apperciation of service rendered by the employee.

Exemption:

- ✓ **Central/ State Government Employees:**
  Any death cum retirement gratuity is **fully exempt** from tax.

- ✓ **Non-Government employees:**
  - ➢ **For employees covered under the Payment of Gratuity Act, 1972-**
    Gratuity is exempt from tax to the extant of <u>least</u> of the following:
    i. ₹ 10,00,000
    ii. Gratuity actually received
    iii. 15 days' salary based on last drawn salary for each completed year of service or *part thereof in excess of 6 months. i.e.*
    $\{\frac{15}{26} \times Last\ drawn\ salary\ \times\ No. of\ competed\ years\ of\ service\ or\ part\ tereof\ in\ excess\ of\ 6\ months\}$

    <u>Note</u> :- For this purpose salary means basic salary and dearness allowance(whether provided in terms of retiring benefit or not)

  - ➢ **For the employees not covered under the Payment of Gratuity Act, 1972-**
    Gratuity is exempt from tax to the extant of <u>least</u> of the following:
    i. ₹ 10,00,000
    ii. Gratuity actually received
    iii. Half month's salary (based on last 10 months' average salary) for each completed year of service. (<u>Fraction is to be ignored</u>)
    $\{\frac{15}{26} \times Last\ drawn\ salary\ \times\ No. of\ competed\ years\ of\ service\ \}$

Note :- For this purpose salary means bassic salary and dearness allowance (if provided in the terms of employement for retireing benefits) and commoission which is expressed as a fixed percentage of turnover.

Notes: -

- Gratuity received during the period of service is fully taxable.
- If gratuity received from 2 or more employer in the same year then aggregate amount of gratuity exempt cannot be exceed ₹10,00,000.
- If gratuity is received in any earlier year from former employer and again received from another employer in a later year, the limit of ₹10,00,000 wii be reduce by the amount of gratuity exempt earlier.
- This exemption is available even if the gratuity is received by the widow, children or dependent of deceased employee.

11. Pension [Section10 (10A)]

Uncommuted Pension: Fully taxable in the hands of both govt. and non-govt. employees.

Commuted Pension: It means lump sum amount taken by commuting the whole or part of the pension.

a) **For Govt. employees :** Fully exempt.

b) **For Non-Govt. employees:**

✓ If employee is in receipt of gratuity –
Exemption = 1/3rd of whole amount of pension.

$$\left\{\frac{1}{3} \times \frac{commuted\ pension\ received}{commutation\%} \times 100\%\right\}$$

✓ If employees does not received any gratuity
Exemption = ½ of the whole amount of pension.

$$\left\{\frac{1}{2} \times \frac{commuted\ pension\ received}{commutation\%} \times 100\%\ \right\}$$

12. Leave Salary [section10 (10AA)]

For Govt. employees : Fully Exempt.

For Non-Govt. employees : Leave salary is exempt from tax to the extent of least of the following:

i. ₹3,00,000,
ii. Leave salary actually received,
iii. 10 month's salary (on the basis of average salary of last 10 month)
iv. Cash equivalent of leave (based of average salary of last 10 month) to the credit of the employee.earned leave entitledment cannot be exceed 30 days for every year.

Notes :

i. salary received during the period of service is fully taxable.
ii. Leave If leave salary received from two or more employer in the same year,then aggregate amount of leave salary exempt from tax cannot exceed ₹3,00,000.
iii. Leave salary received from former employer in any earlier year and again received from another employer in later year, the limit of ₹3,00,000 will bereduce by the amount of leave salary exempt earlier.
iv. Salary means basic salary and dearness allowance(if provided in the terms of retirement benefits) and commission which is express as fixed percentage of turnover.

13. Retrenchment Compensation [saction10 (B)]

$$\frac{15}{26} \times Avg. salary\ of\ last\ 3\ months\ \times completed\ year\ of\ service\ or\ part\ thereof\ in\ excess\ of\ 6\ months$$

OR

₹ 5,00,000

Whichever is lower.

14. Compensation received on Voluntary Retirement (VRS) [Section10 (10C)]

- **Exemption:**
  - ₹5,00,000,
  - Voluntary compensation actually received,
  - Monthly salary × 3 Months × Numbers of completed years of service,
  - Monthly salary (At the time of retirement) × balance months of service.

- This exemption willl be available even if such compensationis received in installments.
- **Conditions :**
  - Employee must completed 10 years of service or completed 40 years of age.
    (This requirement is not applicable in case of an employees of a pubic sector company under the scheme voluntary seperetion framed by the company)
  - The retireing employee of a company shall not be employed in another company or concern belonging to same management.

15. Provident Fund

The tax treatment of provident fund is given below :

Particulars	Recognised PF	Unreconised PF	Statutory PF	Public PF
Emplpyers contribution	Amount in excess of 12% of salary is taxable.	Not taxable yearly	Fully exempt.	N.A. (as there is only assessee's own contribution)
Employee's Contribution	Eligible for deduction u/s 80C	Not eligible for deduction	Eligible for deduction u/s 80C	Eligible for deduction u/s 80C
Interest Credited	Amount in excess of 9.5% p.a. is taxable	Not taxable yearly	Fully exempt	Fully exempt
Amount received on retirement, etc.	See Note (i), (ii)	See Note (v), (vi)	Fully exempt u/s 10(11)	Fully exempt u/s 10(11)

Notes:

i. Amount received on maturity of RPF is fully exempt in case of an employee who has rendered continuous services for a period of 5 years or more.
ii. If termination taken place within 5 years then amount received would be fully exempt only if the services had been teminated due to employees health or discontinuance or contraction or employer's business or other reason beyond the control of employee.
iii. If an employee, after termination of his employment with one employer, obtain the employment under another employer,then so much of accumulated balance in his provident fund account will be exempt which is transferred to his individual account in a recognised provident fund maintaied by the new employer.
iv. In such case, the period of service with the former employer shall also be taken into acocunt for computing the period of five years' continuous service.
v. Employee's contribution is not taxable but interest thereon is taxable unde 'Income from Other Sources'.
vi. Employer's contribution and interest thereon is taxable as salary.
vii. Salary means : Basic Salary + Dearness Allowances (If provided in the terms of employment) + commission (If provided as a percentage of turnover).

16. Approved Superannuation Fund

The tax treatment of contribution and exemption of paymentfrom tax are as follows:

i. Employers contribution is exempt from tax in the hands of employees **upto ₹1,00,000 per employee per annum**.
ii. Employees's contribution qualifies for deduction under section 80C.
iii. Interest on accumulated balance is exempt from tax.

17. Salary from United Nations organisation

Salaries and emoluments, Pension received from UNO under United Nation Act, 1947 is **exempt** from tax.

18. Allowances

Allowances		
Fully Taxable	**Partly Taxable**	**Fully Exempt**
i. Entertainment Allowance ii. Dearness Allowance iii. Overtime Allowance iv. Fixed Medical Allowance v. Fixed Medical Allowance vi. City Compensatory Allowance vii. Interim Allowance (to meet increased cost of living in cities) viii. Servent Allowance ix. Project Allowance	i. House Rent Allowances [u/s 10(13A)] ii. Special Allowances [u/s 10(14)]	i. Allowances granted to Government employees outside India. ii. Stamptury Allowances granted to high Court or supreme Court Judges. iii. Allowances paid by the United Nations Organisation. iv. Compensatory Allowances received by a Judge.

x. Tiffin/ Lunch/ Dinner Allowance xi. Any Other Cash Allowance xii. Warden Allowance xiii. Non-practicingAllowances		

Allowances which are partially taxable:

i. **House rent allowances [Section 10(13A)]:** HRA granted to an employee is exempt to the extant of least of the following:

Metro Cities(i.e. Delhi, Kolkata, Mumbai, Chennai)	Other Cities
1) HRA actually received.	1) HRA actually received.
2) Rant paid – 10% of salary for the relevent period.	2) Rant paid – 10% of salary for the relevent period.
3) 50% of salary for the relevent period.	3) 40% of salary for the relevent period.

Notes:

i. Exemption is not available to an assessee who lives in his own house, or in a house for which he has not paid any rent.

ii. Salary means = Basic Salary + Dearness Allowances (If provided in the terms of employment) + commission (If provided as a percentage of turnover).

ii. **Special Allowances [Section 10(14)(ii)]:**

- **Special compensatory**(*Tribal Areas/ Schedule Areas/ Agency Areas*) **Allowance** - ₹ 200 per month.
- **Children Education allowances** - ₹ 100 per month per child up to two children.
- **Children Hostal Expenditure Allowance** - ₹ 300 per month per child upto a maximum of two children.
- **Transport Allowance -** For the purpose of communicating between the place of his residence and place of his duty - ₹ 1,600 per month.
  To an employee who is blind or orthopaedically handicapped with disability of the lower extremities of the body - ₹ 3,200 per month.

19. Perquisites

i. **Valuation of Rent-Free Concessional Accommodation –**

SI. No.	Circumstances	Unfurnished Accommodation	Furnished Accommodation
(1)	**(2)**	**(3)**	**(4)**
1	Where accommodation provided by government	License fee determined by government as reduce by the rent	Value of perquisite as determined under column (3) **+** 10% per annum of the cost of furniture.

		actually paid by the employee.	If such accommodation taken on hire, the actual hire charges payable reduce by any amount paid or payable
2	Where the accommodation is provided by any other employer – **i.** Where accommodation is owned by the employer – **a)** In cities having population up to **10 lakh** b) In cities having population **exceeding 10 lakh and up to 25 lakh** c) In cities having population **exceeding 25 lakh** **ii.** Where accommodation is taken on lease or rent by the employer	**- 7.5 %** of salary **- 10 %** of salary **- 15 %** of salary **Actual lease rent** paid payable Or **15 % of salary** Whichever is **lower** As reduce by the amount actually paid by the employee	Value of perquisite as determined under column (3) **+** 10% per annum of the cost of furniture. If such accommodation taken on hire, the actual hire charges payable reduce by any amount paid or payable
3	Where accommodation provided by any employer in a **Hotel.**	Not Applicable	**24 % of salary** Or **Actual Charges** Whichever is Lower As reduce by the amount recovered from employee. However if such accommodation provided for a period not exceeding fifteen days on the account of transfer from one place to another, there would be no perquisite

Notes:

- "Salary" includes pay, allowances, bonus or commission payable monthly or otherwise but it does not include following-
  a) Dearness allowances if not in terms of retiring benefits;
  b) Employer's contribution to the provident fund of employee;
  c) Allowances which are exempted from tax;

d) Perquisite value of Rent-Free Accommodation;
e) Any other expenses which are specifically excluded from payment of tax.

- If an employee provide any accommodation on the account of his transfer from the one place to another, at the new place of posting while retaining the accommodation at the other place, the perquisite value shall be determined with the reference to only one such accommodation which has lower perquisite value for a period of 90 days and thereafter, the value shall be charged for both such accommodations.

ii. **Motor Car:**

Perquisite value of motor car will be determined as under

A. **Where the motor car is owned or hired by employer** –

Sl No.	Circumstances	Engine Cubic Capacity	
		Up to 1.6 litres	**Exceed 1.6 litres**
1.	Used wholly or exclusively in the performance of his official duties	Not a perquisite	Not a perquisite
2.	Used exclusively for the private or personal purpose of employee	Expenditure incurred by the employer on running and maintenance **+** chauffeur	Expenditure incurred by the employer on running and maintenance **+** chauffeur
3.	Used partly in the performance of duties and partly for private or personal purpose		
	a) If running and maintenance are met or reimburse by **employer**	**₹1,800** + ₹ 900 (if chauffeur is provided)	**₹ 2,400** + ₹ 900 (if chauffeur is provided)
	b) If running and maintenance are met or reimburse by **assesse/ employee**	**₹ 600** + ₹ 900 (if chauffeur is provided)	**₹ 900** + ₹ 900 (if chauffeur is provided)

B. **Where Motor Car is owned by employee but running and maintenance charges are met by employer** -

Sl No.	Circumstances	Engine Cubic Capacity	
		Up to 1.6 litres	**Exceed 1.6 litres**
1.	Used wholly or exclusively in the performance of his official duties	Not a perquisite	Not a perquisite
2.	Used partly in the performance of duties and partly for private or personal purpose	Amount actually incurred – **₹1,800** + ₹ 900 (if chauffeur is provided)	Amount actually incurred – **₹ 2,400** + ₹ 900 (if chauffeur is provided)

Note: If more than one Motor Car is provided, then perquisite value shall be calculated only in respect of one car as per above rules and other cars are treated as used wholly for personal purpose.

iii. **Valuation of benefit of provision of domestic servant:**
Perquisite value shall be actual cost to employer (Salary to servant) reduce by the amount recovered from employee.

iv. **Valuation of gas, electricity or water supplied by employer:**
- Perquisite value shall be the sum equal the actual cost to employer.
- If such resources are owned by employer, then perquisite value shall be the manufacturing cost per unit incurred by the employer.

Reduce by amount recovered from employer.

v. **Valuation of free or concessional education educational facilities:**
- Value of such benefit shall be equal to the amount of expenditure incurred by employer on this behalf.
- Where educational institution is maintained and owned by employer, the value of benefit shall be the cost of such education in a similar institution in or near locality
- Such value shall be reduce by the amount recovered from employer
- However, there would be **no perquisite** if cost of such educational facility per child is **not exceeding ₹ 1,000 per month.**

vi. **Free or concessional tickets:**
Where an employer who is engage in business of carriage of passengers or goods,
Provide to any employee or to any member of his household,
Personal or private journey free of cost or at concessional fare,
In any conveyance owned or leased or any other arrangement,
The value of perquisite shall be the value at which such benefits are offered by employer to public as reduce by amount recovered from employee.

vii. **Interest-free or concessional loan:**
Value of such benefit shall be determined as sum equal to the interest computed at the rate charged per annum by the State Bank of India, as on the 1^{st} day of the relevant previous year on the maximum outstanding balance reduce by the amount of interest received.

However, there would be **no perquisite** if such loan is taken for the purpose of medical treatment of prescribed diseases (like Cancer) or where amount of loan **not exceeding ₹ 20,000** in aggregate.

viii. **Travelling, touring and accommodation:**
- Value of such benefit shall be sum equal to the amount of the expenditure incurred by employer in this behalf.
- If such facility is maintained by the employer and not available uniformly to all employee, the value of benefit shall be taken to be the value at which such facilities are offered by other agencies to the public.
- Where an employee is on official tour and expenses incurred in respect of any member accompanying him, the such expenses is also treated as fringe benefit
- Where an official tour is extended as vocation, then fringe benefit shall be limited to only such extended period.

ix. Free or concessional food and non-alcoholic beverages:

- Value of benefit shall be amount of expenditure incurred by employer.
- However, there would be no perquisite if –
    a. Amount of such expenditure is not exceeding ₹ 50 per meal or
    b. Tea or snacks provided during working hour or
    c. Provided in a remote area or off-shore area.

x. Value of gift, voucher or token:

No perquisite up to ₹ 5,000 I aggregate during the previous year. If exceeding ₹ 5,000 amount actually incurred.

xi. Credit card expenses: Amount of expenditure incurred by employee as reduce by the amount received from employee.

xii. Club expenditure: Amount of expenditure incurred by employee as reduce by the amount received from employee.

xiii. Use of movable assets:

Asset given	Value of benefit
1. Use of laptop and computer	**Nil**
2. Movable asset , other then – **a.** Laptop and computers; and **b.** Assets already specified	**10% p.a.** of actual cost of such asset **Or** The amount of rent or charges paid or payable by the employer, **As the case may be**

xiv. Transfer of movable assets:

Assets transferred	Value of perquisite
computers and electronic items	Depreciated value of asset [Depreciation is computed @ **50% on WDV** for each completed year of usage]
Motor-Cars	Depreciated value of asset [Depreciation is computed @ **20% on WDV** for each completed year of usage]
Any other Asset	Depreciated value of asset [Depreciation is computed @ **10% on SLM** for each completed year of usage]

xv. Value of sweat equity shares:

A. In case of listed shares:

- In a case where, on the date of exercising the option, the share of the company is listed on a recognised stock exchange, the fair market value shall be the average opening and closing price of the share on that date on the said stock exchange
- If shares are listed more than one recognised exchange, the fair value shall be the average of opening and closing price of that recognised exchange which records highest volume of trading in shares.

- If on the date of exercising, there is no trading-
  - Fair market value shall be closing price of any recognised stock exchange.
  - If listed in more than one recognised stock exchange, closing price of that stock exchange which records highest volume of trading.

B. If shares are not listed:
Value shall be determined by **merchant banker**.

xvi. Value of securities other than shares:
As determined by Merchant Banker.

xvii. Medical facilities:

- Fully exempt:
  - In a hospital maintained by employer.
  - In government hospital.
  - Treatment of prescribed disease in a hospital approved by chief commissioner.
  - Insurance premium paid by employer on health of employee (Approved by IRDA
- There would be **no perquisite up to expenditure ₹ 15,000.**
- If medical treatment is outside India –
  - Medical treatment + Travel and Stay abroad of employee or any member of his household + Travel and Stay abroad of one attendant.
  - It will be **exempt** only to **extant permitted by the RBI.**
  - Travelling of patient and attendant is exempt if employee's gross total income as computed before including the said expenditure is not exceeding ₹ 2 lakh.
  - Family means spouse and children + parents (Wholly or mainly dependent).

20. Deductions from Salary

i. Entertainment Allowance [Section 16(ii)]:

- **Non-govt. employees:** Fully taxable
- **Government employees:** Deduction will be lower of following -
  - **a.** 20 % of salary (one fifth) or
  - **b.** ₹ 5,000 or
  - **c.** Entertainment allowance received.
- Entertainment allowances first to be included in salary and then allowed as deduction.

ii. Professional Tax:

- Deduction is allowed only when actually paid.
- Paid by employer is first to be included in salary and then allowed as deduction.