

UDHNA COLLEGE

SYBCOM SEM-IV

ADVANCED ACCOUNTING & AUDITING-IV

(Accountancy & Taxation)

Unit 2 Computation of Income under the Head “Salaries”(20%)

• **Meaning**

The meaning of the term ‘salary’ for purposes of income tax is much wider than what is normally understood. The term ‘salary’ for the purposes of Income-tax Act, 1961 will include both monetary payments (e.g. basic salary, bonus, commission, allowances etc.) as well as non-monetary facilities (e.g. housing accommodation, medical facility, interest free loans etc.).

Section 17(1) defined the term “Salary”. It is an inclusive definition and includes monetary as well as non-monetary items.

‘Salary’ under section 17(1), includes the following:

1. wages,
2. any annuity or pension,
3. any gratuity,
4. any fees, commission, allowances, perquisite or profits in lieu of or in addition to any salary or wages,
5. any advance of salary,
6. any payment received in respect of any period of leave not availed by him i.e. leave salary or leave encashment,

7. Provident Fund: - any contribution to the RPF by the employer, in excess of 12% of employee's salary and any interest credited to RPF in excess of 9.5% p.a.
8. The contribution made by the Central Government or any other employer in the previous year to the account of an employee under a pension scheme referred to in section 80CCD.

- **Basis of charge (Section 15)**

- Section 15 deals with the basis of charge. Salary is chargeable to tax either on 'due' basis or on 'receipt' basis, whichever is earlier.
- However, where any salary, paid in advance, is assessed in the year of payment, it cannot be subsequently 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.

Points to consider:

- a) Salary income is chargeable to tax on "due basis" or "receipt basis" whichever is earlier.
- b) Existence of relationship of employer and employee is must between the payer and payee to tax the income under this head.
- c) Income from salary taxable during the year shall consists of following:
 - i. Salary due from employer (including former employer) to taxpayer during the previous year, whether paid or not;
 - ii. Salary paid by employer (including former employer) to taxpayer during the previous year before it became due;
 - iii. Arrear of salary paid by the employer (including former employer) to taxpayer during the previous year, if not charged to tax in any earlier year;

- **Calculation of income under the head salary**

Basic Salary	—
Add:	—
1. Fees, Commission and Bonus	—
2. Allowances	—
3. Perquisites	—
4. Retirement Benefits	—
Gross Salary	—
Less: Deductions from Salary u/s 16	—
Standard Deduction	75000
Net Taxable Salary	—

- **Allowances**

Allowance is a fixed monetary amount paid by the employer to the employee for meeting some particular expenses, whether personal or for the performance of his duties. These allowances are generally taxable and are to be included in the gross salary unless a specific exemption has been provided in respect of any such allowance. Specific exemptions in respect of allowances are provided under the following sections:

I. House Rent Allowance-Section 10(13A)

II. Prescribed Special Allowances - Section 10(14):

(i) Special Allowances for performance of official duties:

- a. Travelling allowance
- b. Daily allowance
- c. Conveyance allowance
- d. Helper allowance
- e. Academic allowance
- f. Uniform allowance

(ii) Allowances to meet Personal Expenses

- A. Children education allowance:
- B. Hostel expenditure allowance:
- C. Tribal area, Scheduled Area/Agency area allowance:
- D. Special compensatory hilly area allowance or high altitude allowance etc.:

E. Border area, remote area allowance, disturbed area allowance, etc.:

F. Compensatory field area allowance:

G. Compensatory, modified field area allowance:

H. Counter insurgency allowance granted to members of armed forces:

I. Underground allowance:

J. High altitude (uncongenial climate) allowance:

Important Note:

As per notification dated 26/6/2020 an employee will get following exemption:

- Any allowance granted to meet the cost of travel on tour or on transfer.
- Any allowance, whether granted on tour or for the period of journey in connection with transfer, to meet the ordinary daily charges incurred by an employee on account of absence from his normal place of duty.
- Any allowance granted to meet expenditure incurred on conveyance in performance of duties of an office or employment of profit. (provided that free conveyance is not provided by the employer)
- Transport allowance up to Rs.3200 p.m. granted to employee, who is blind or deaf and dumb or orthopaedically handicapped with disability of lower extremities, to meet his expenditure for the purpose of commuting between the place of his residence and the place of his duty.

- **Perquisites Sec.17(2) (perk)**

Perquisite may be defined as any casual emolument or benefit attached to an office or position in addition to salary or wages. It also denotes something that benefits a man by going into his own pocket. Perquisites may be provided in cash or in kind.

TYPES OF PERQUISITES:

- **Tax-exempted Perquisites**

Some of the fringe benefits like company-provided laptops and computers, employer-provided refreshments during office hours, etc., are non-taxable. Besides, telephone or mobile bills, recreational and free medical facilities, etc., are also counted as tax-exempted perquisites.

- **Taxable Perquisites**

Employee-provided benefits like water and electricity, medical expense reimbursements, rent-free accommodation, gas supply, etc., are perquisites taxable. Moreover, the salary of the employee's servants, other benefits like gifts above Rs 5000, free meals, gym and club facilities, etc., come under taxable perquisites.

- **Perquisites Taxable only for specified Employees**

- Value of any benefit or perquisite provided for free or at a concessional rate which is not included in the above two kinds will be taxable in the hands of specified employees.

Specified Employees include;

- Director Employee, i.e. an employee who is also a director in the company.
- Employees having substantial interest (has more than 20% of the voting power).
- Employees whose gross salary exceeds Rs 50,000

Valuation of Perquisites:

- **Fringe Benefits Or Amenities Which Shall Be Taxable Perquisites In The Hands Of All Employees:**

1. Valuation of Perquisite in respect of Interest-Free Loan or Loan at Concessional Rate of Interest [Section 3(7)(i)]

If a loan is given by an employer to the employee (or any member of his household), it is a perquisite chargeable to tax. It is taxable on the following basis—

1. **Step 1** : Find out the “maximum outstanding monthly balance” (i.e., the aggregate outstanding balance for each loan as on the last day of each month).
2. **Step 2** : Find out rate of interest charged by the State Bank of India (SBI) as on the first day of the relevant previous year in respect of loan for the same purpose advanced by it.
3. **Step 3** : Calculate interest for each month of the previous year on the outstanding amount mentioned in Step 1 at the rate of interest given in Step 2.
4. **Step 4** : From the total interest calculated for the entire previous year under Step 3, deduct interest actually recovered, if any, from the employee during the previous year.
5. **Step 5** : The balance amount [i.e. Step 3 minus Step 4] is taxable value of the perquisite.

2. Valuation of Perquisites in respect of Travelling, Touring, Accommodation [Rule 3(7)(ii)]

The basis of valuation is as follows—

<i>Mode of Valuation</i>	<i>Perquisite in respect of travelling, touring, accommodation and any other expenses paid by employer for any holiday availed by employee (or any member of household) other than leave travel concession.</i>	
	<i>Where such facility is available only to all employees</i>	<i>Where such facility is not available uniformly to all employees</i>
Step 1 - Find out cost to the Employer	Expenditure incurred by the Employer	Value at which such facilities are offered by other agencies to the public.
Step-2 : Less : Amount recovered from the Employee	Recovered from the Employee	recovered from the Employee
Taxable Value of Perquisites (Step 1 - Step 2)	Balancing amount (if it is positive).	Balancing amount (if it is positive).

3. Valuation of Perquisites in respect of Lunch / Refreshment, etc. [Rule 3(7)(iii)]

If any lunch allowance, dinner allowance or refreshment allowance is given to an employee, it is chargeable to tax.

The value of free meals provided by the employer is taxable as follows—

<i>Mode of Valuation</i>	<i>Food and Non-alcoholic beverages is provided in working hours in remote area or in an offshore installation.</i>	<i>Lunch / Refreshment is provided in working hours or extended working hours at any other place</i>	
		<i>Tea, Snacks, and Non-alcoholic beverages in office premises</i>	<i>Food in office premises or through non-transferable paid voucher usable only at eating joints.</i>
Step 1 : Find out Cost to the Employer	NIL	NIL	Cost to the Employer in excess of Rs.50 per meal.
Step-2 : Less : Amount recovered from the Employee	NIL	NIL	Recovered from the Employee

Taxable Value of Perquisites (Step 1 - Step 2)	NIL	NIL	Balancing amount (if it is positive).
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4. Valuation of Perquisites in respect of Gift, Voucher or Token [Rule 3(7)(iv)]

Tax Treatment :

(A) Aggregate Value of Gift is up to Rs. 5000 during the previous year :

- Perquisites Value is NIL

(B) Aggregate Value of Gift is more than Rs. 5000 during the previous year :

- Perquisites Value is the value in excess of Rs. 5000

NOTE: If gift is given in cash or by way of cash cheque which can be converted into cash, the entire amount received is taxable.

5. Valuation of Perquisites in respect of Credit Card Facilities [Rule 3(7) (v)]

The perquisite in respect of credit card is taxable as follows—

(A) Used for Personal or Private Purposes:

Perquisites Value is equal to Expenses, Membership Fees and Annual Fees incurred by the Employee and Reimbursed / Paid by the Employer.

(B) Used wholly and exclusively for Official Duties

Perquisites Value is NIL

6. Valuation of Perquisites in respect of Club Expenditure or Membership [Rule 3(7) (vi)]

Employers often extend membership of reputed Clubs to senior Corporate Employees and they can use the same for Private or Official purposes or for Both.

The perquisite in respect of club facility is taxable as follows—

(A) Used for Private Purpose

Perquisites value is the expenditure incurred by employer including the amount of annual or periodical Fee

(B) Used for discharged of Official Duties

Perquisites Value is NIL

(C) Provision of Health Club, Sports Club, etc. facilities to all employees uniformly

Perquisites Value is NIL.

7. Perquisites in respect of Use of Employer's Movable Assets [Rule 3(7)(vii)]

The value of benefit to the employee results from the use by the employee or any member of his household of any moveable asset (Excluding Laptop & Computer) belonging to the employer or hired by him shall be determined as under:

Tax Treatment:

(A) When the Movable Assets is owned by the Employer:

- Value of Perquisites is 10% per annum of the actual cost of the Asset

(B) When the Movable Asset is hired by the Employer:

- Perquisites Value is Rent/Hire Charges Paid / payable by the Employer.

8. Valuation of the Perquisites in respect of Movable Assets sold by an Employer to its Employees at a Nominal Price [Rule 3(7) (viii)]

The value of benefit to the employee arising from the transfer of any moveable asset belonging to the employer directly or indirectly to the employee or any member of his household shall be determined as under:

Tax Treatment:

(A) If Movable Assets are Computers and Electronic Items:

Perquisite Value is the difference between the Actual cost of assets as reduced by 50% (Reducing Balance Method) for each completed year from the period it was put to use and the amount paid by the employee.

(B) If Movable Assets are Motor Cars:

Perquisite Value is the difference between the Actual cost of assets as reduced by 20% (Reducing Balance Method) for each completed year from the period it was put to use and the amount paid by the employee.

(C) In case of any Other Movable assets:

Perquisite Value is the difference between the Actual cost of assets as reduced by 10% (SLM) of cost for each completed year from the period it was put to use and the amount paid by the employee.

B. Perquisites which are Taxable in case of Specified Employees

1. Valuation of Perquisites in respect of Motor Car and other Modes of Conveyance [Rule 3(2)]

1. When the Motor Car is Owned or Hired by the Employer

(A). Motor Car is used wholly and exclusively in the performance of Official Duties:

- Perquisites Value is NIL

(B) Motor Car is used exclusively for Private / Personal Purposes:

- Perquisites value is actual Expenditure incurred by the employer on the running and maintenance of Car + Salary of Chauffeur + Normal Wear and Tear (i.e. 10% p.a. of the Vehicle Cost) or Hire Charges.
- In case Expenses on Maintenance and running are met by the Employee: Perquisites Value is confined to Salary paid to Chauffeur and normal Wear and Tear (i.e. 10% p.a. of the Vehicle Cost).
- If any amount is recovered from employee the same shall be deducted from the Perquisite Value.

C. Motor Car is Used Partly in the performance of Duties and Partly for Private / Personal Purposes.

1. When CC does not exceed 1600 CC :

- When Expenses on maintenance and running are met by the Employer:
 - Perquisites Value is Rs. 1800 p.m. (plus Rs.900 if Chauffeur is provided)
- When Expenses on maintenance and running are met by the Employee:
 - Perquisites Value is Rs. 600 p.m. (plus Rs.900 if Chauffeur is provided)

- If any amount is recovered from employee is Not Deductible

2. When CC exceed 1600 CC:

- When Expenses on maintenance and running are met by the Employer:
 - Perquisites Value is Rs. 2400 p.m. (plus Rs.900 if Chauffeur is provided)
 - If any amount is recovered from employee is Not Deductible
- When Expenses on maintenance and running are met by the Employee:
 - Perquisites Value is Rs. 900 p.m. (plus Rs.900 if Chauffeur is provided)
 - If any amount is recovered from employee is Not Deductible

2. When the Motor Car is owned by the Employee

1. When Expenses on maintenance and running are met by the Employee:

- Perquisites Value is NIL

2. When Expenses on maintenance and running are met or Reimbursed by the Employer:

(A) Motor Car is used wholly and exclusively in the performance of Official Duties:

- Perquisites Value is NIL

(B) Motor Car is used partly in the performance of Official Duties and Partly for Private / Personal purposes:

- When the CC of Motor Car does not exceed 1600 CC :-
 - Perquisites value is Actual Expenditure incurred by the Employer as Reduced by the amount of Rs. 1800 p.m. plus (+) Rs.900 p.m. if chauffeur is provided
Less amount recovered from the employee.

- When the CC of Motor Car exceed 1600 CC :-
 - Perquisites value is Actual Expenditure incurred by the Employer as Reduced by the amount of Rs. 2400 p.m. plus (+) Rs.900 p.m. if chauffeur is provided Less amount recovered from the employee.

(C) Motor Car is used exclusively for Private Purposes

- Perquisites value is Actual Expenditure incurred by the Employer Less amount recovered from the employee.

2. Valuation of Perquisites in respect of Free Domestic Servants [Rule 3(3)]

The value shall be the actual cost to the employer i.e. the total amount of salary paid or payable by the employer or any other person on his behalf for such services as reduced by any amount paid by the employee for such services.

3. Valuation of Perquisite in respect of Gas, Electricity or Water Supply provided Free of Cost [Rule 3(4)]

The Valuation is explained in the following chart:

Circumstances	Value of Benefit
(a) Where such supply is made from resources owned by the employer without purchasing from the outside agency	It shall be the manufacturing cost per unit incurred by the employer
(b) In any other case	Amount paid on this account by the employer to the agency supplying the gas, electric energy or water

However, in both the above cases, if employee is paying any amount in respect of such services, the amount, so paid, shall be deducted from the value so arrived at.

4. Educational facility for children of the employee:

Where the educational institution itself is maintained and owned by the employer and free educational facilities are provided to the children of the employee or where such free educational facilities are provided in any institution by reason of his being in employment of that employer, there shall be **no perquisite value** if the cost of such education or the value of such benefit per child does not exceed ₹1,000 p.m.

5. Rent Free Accommodation:

Types of Rent-Free Accommodation

There are two types of rent-free accommodation as offered by the central government, state government, private and other companies:

- **Furnished Rent Free Accommodation**
- **Unfurnished Rent Free Accommodation**

Rent-Free Accommodation Taxability

Taxability of RFA/CRA has undergone amendment recently and the changes are effective from September 1, 2023. Taxability depends on various factors such as type of employer, city in which accommodation is provided, salary of employee, etc. Here is the procedure for calculating income tax on rent-free accommodation as per accommodation type:

- **Unfurnished Rent-free Accommodation**

In the case of unfurnished rent-free accommodation, the perquisite value is calculated as follows:

Employer	City Population as per 2011 census	New Rates (w.e.f. 01.09.2023)
Government	NA	License fee determined by the government
Other than Government (Owned by Employer)	Upto 15 Lakh	5% of Salary
	15 Lakh to 40 Lakh	7.5% of Salary
	Above 40 Lakh	10% of Salary

- **For properties taken on lease by an employer, the value of perquisite is lower of:**
 - (i) Actual lease rental as paid by an employer
 - or
 - (ii) 10% of an employee's salary.
- **Furnished Rent-free Accommodation**

Furnished rent-free accommodation includes modern amenities like television, furniture, air-conditioner, etc. In the case of such accommodation, if furniture is owned by employer an additional 10% of the actual price of the amenities is added as a perquisite. If furniture is hired by the employer then the actual hire charges are to be added as a perquisite.

- **Taxability of Hotel Accommodation as Provided by the Employer**

When an employer offers housing to an employee for less than 15 days, it would not be taxable, if employer provides hotel accommodation for 15 days and above as RFA/CRA, the value of perquisite is computed as follows:

1. 24% of the salary

OR

2. Actual charges payable or paid to the hotel (whichever is lower)

This is only applicable to permanent employees. Temporary employees sent to a location for project execution or accommodated at offshore sites do not count. Thus, the following requirement is applicable if an employee gets accommodation at a new place due to transfer while retaining existing accommodation:

Tax Exemption on Rent-Free Accommodation

- If the accommodation is provided in a remote area, it is not taxable as per the law.
- When your company accommodates you in a hotel for less than 15 days due to your transfer, the perquisite value shall be eligible for tax exemption.
- If a rent-free accommodation is provided to a member of UPSC. In that case, Supreme Court Judge Union Minister, Parliament official, High Court Judge, Leader of Opposition in Parliament, etc., it does not come under taxable perquisite.

What is the definition of salary?

In regards to the taxability of rent-free accommodation, salary is defined as a total of the following:

- Basic pay

- DA(only if enters into retirement benefits)
- Bonus
- Commission
- All taxable allowances, etc.

C. Perquisites Exempted from Tax for all Employees and Not Added in Salary Income

1. Medical facility:

The value of any medical treatment provided to an employee or any member of his family in a hospital, dispensary or a nursing home maintained by the employer shall be a tax free perquisite.

2. Recreational facilities:

Any recreational facility provided to a group of employees (not being restricted to a select few employees) by the employer is not taxable.

3. Training of employees:

Any expenditure incurred by the employer, for providing training to the employees or by way of payment of fees of refresher courses attended by the employees.

4. Use of health club, sports and similar facilities provided uniformly to all employees by the employer.

5. Expenses on telephone, including a mobile phone, actually incurred on behalf of the employee by the employer.

6. Employer contributions to the employee's recognized Provident Fund (PF), Employee Provident Fund (EPF), National Pension System (NPS), and superannuation fund up

to Rs 7,50,000 are exempt from tax, subject to specific limits. Any surplus amount will be taxable under section 17(2)

7. The premium paid by the employer on an accident policy taken out by it in respect of the employee would not be a perquisite.
8. Amount given by employer of assessee to assessee's child as scholarship is exempt under section 10(16).
9. Laptop & Computer

- **Retirement Benefits:**

1. Taxability of Pension

Pension is any amount of periodic payment made by an employer to the employee in consideration of past service payable after retirement.

Pension is of two Kinds:-

Uncommuted Pension:-

Uncommuted pension is pension received periodically. It is fully taxable in the hands of both government and non government employees.

Commutated Pension:-

Commutated pension means lump sum amount taken by commuting the whole or part of the pension

- Commuted pension received by employees of the central government/local authorities/statutory corporation/members of the defence services is fully exempt from tax.

- Commuted pension received by non government employees is taxable subject to exemption u/s 10(10A) of the Income Tax Act, 1961 as under:-

a) Where the employee has also received gratuity

One-third(1/3) of pension which is normally entitled to receive is exempt from tax

b) Where the employee has not received gratuity

Half (1/2) of pension which is normally entitled to receive is exempt from tax

2. Taxability of Gratuity

Gratuity is a voluntary payment made by an employer in appreciation of services rendered by an employee.

- Any death cum retirement gratuity received by Central/State government employees is fully exempt.
- Any gratuity received by an employee during the period of service is fully taxable.

Gratuity received by Non government Employee

Gratuity received by non government employees is fully taxable under the income tax act 1961 subject to exemption provided by sec 10(10) which is described as under:-

Where the employee is covered by payment of gratuity act 1972:-

Least of the following is exempt:-

a) Rs 20,00,000

b) Gratuity received

c) $15/26$ * Last drawn salary * number of completed year of service or part thereof in excess of 6 Months (Where an employee has worked for 8 years 7 months, the completed year of service shall be considered 9)

Note: Salary for this purpose means: Basic Salary + Dearness Allowance

Where the employee is not covered by the Payment of Gratuity act 1972:-

Least of the following is exempt:-

a) Rs 20,00,000

b) Gratuity received

c) $1/2$ * Average salary of last 10 months * completed year of service (where an employee has worked for 8 Years 7 Months, the completed years shall be considered as 8)

Note: Salary for this purpose means Salary + Dearness allowance (If provided in terms of employment for retirement benefits) + commission as a % of turnover.

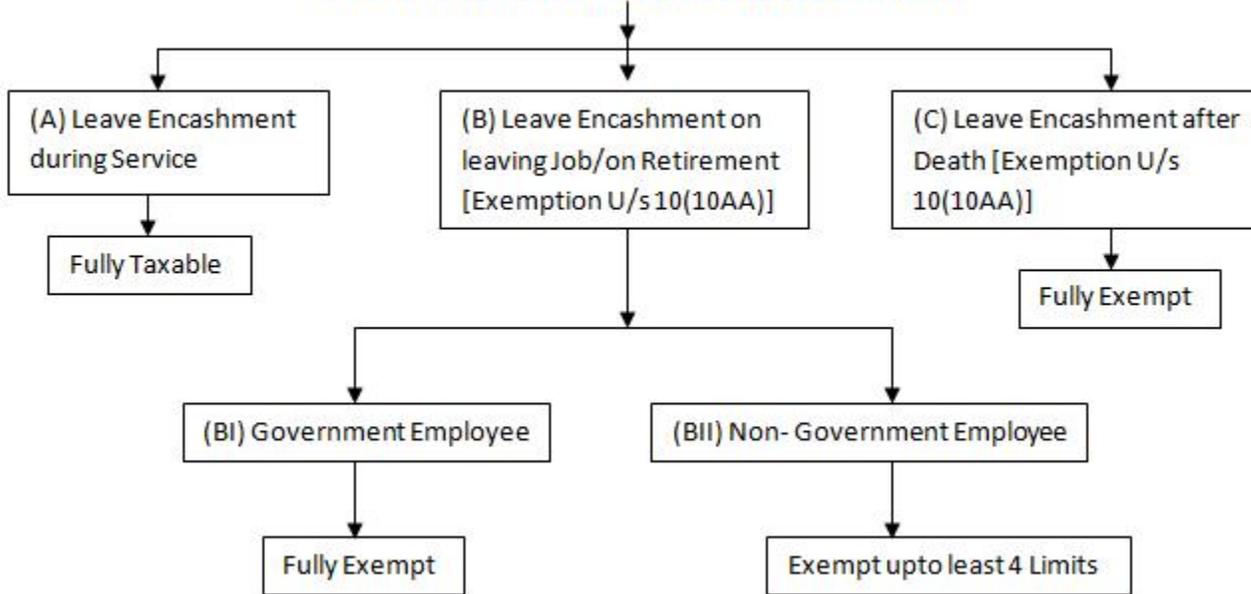
3. Leave Encashment [Section-10(10AA)] :

As per terms of employment, generally, an employee is granted certain period of leave(s) on yearly basis. Such leave(s) may be casual leaves, medical leaves and privileged leaves or earned leaves. Generally, an employee can accumulate his medical leaves and privileged leaves and can avail such leaves in subsequent years as per his necessity.

However, in some cases, an employee can even encash his accumulated privileged/earned leaves and can get salary for the said period of leave. Such receipt of salary by an employee from his employer in lieu of his accumulated leaves is called "Leave Encashment".

Such encashment can be done by an employee either during the service or at the time of leaving job due to retirement or any other reason. However, in case of death of an employee, the salary for his/her accumulated leave is given to his/her legal heirs.

Tax Treatment of Leave Encashment



(A) Leave Encashment during service.

Any encashment of leaves by an employee during continuance of service is “fully taxable” for all employees whether government employees or non- government employees. Such encashment may either be of current year leaves or of past accumulated leaves. It is taxable as salary income of the employee for the previous year in which amount is received by employee.

(B) Leave Encashment on Leaving Job / Retirement

(BI) For Government Employees [Section 10(10AA)(i)].

Any payment received as leave encashment at the time of retirement or on leaving job otherwise shall be “**Fully Exempt**” u/s 10(10AA)(i).

Meaning of Government Employee. Government employee includes

- a. Employees of Central Government
- b. Employees of state Government

For Non-Government Employees [Section 10(10AA)(ii)].

Any payment received as leave encashment at the time of retirement or on leaving job otherwise shall be exempt upto the least of following amounts Under Section 10 (10AA)(ii).

Minimum of the following four limits:

- i. Leave encashment actually received; or
- ii. 10 months average salary; or
- iii. Cash equivalent of unavailed leave calculated on the basis of maximum 30 days leave for every year of actual service rendered; or
- iv. Rs. 25,00,000(w.e.f.1/4/23)

NOTE:

1. Salary includes DA to the extent the terms of employment so provide and fixed percentage commission on turnover.