



# SALARIES



## LEARNING OUTCOMES

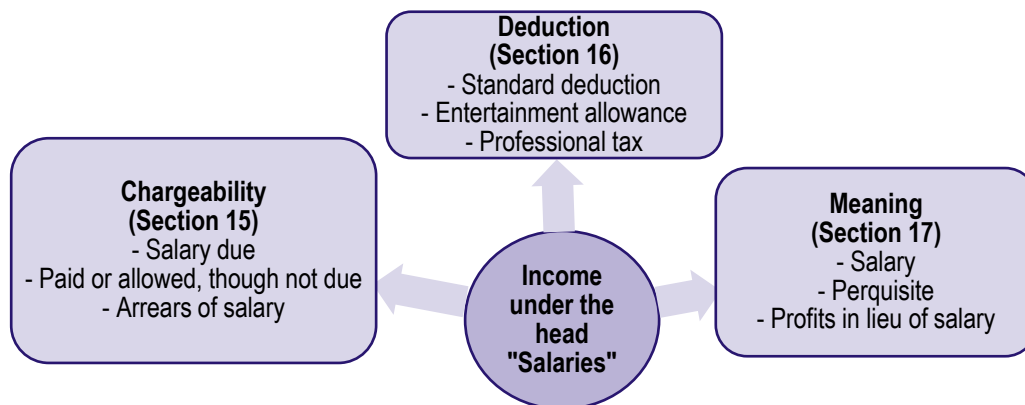
After studying this chapter, you would be able to -

- ❑ **appreciate** the meaning of the terms “Salaries”, “Profits in lieu of salary”, allowances, and “Perquisites”;
- ❑ **examine** whether a particular receipt/ income would constitute salary taking into consideration the nature of relationship between the payer and payee;
- ❑ **compute** the value of taxable allowances, perquisites, terminal or retirement benefits;
- ❑ **compute** the income chargeable under the head “Salaries” after allowing standard deduction and deductions available in respect of entertainment allowance or professional tax, if any, and determine tax liability thereon;
- ❑ **formulate** the ideal salary structure to minimise the overall tax liability on income under the head “Salaries”.



## 4.1 INTRODUCTION

The provisions pertaining to Income under the head “Salaries” are contained in sections 15, 16 and 17.



Let us now recap the important concepts relating to Salaries.

- (1) **Employer-employee relationship:** Every payment made by an employer to his employee for service rendered would be chargeable to tax as salaries. Before an income can become chargeable under the head 'salaries', it is vital that there should exist between the payer and the payee, the relationship of an employer and an employee.

**Example 1:** Sujata, an actress, is employed in Chopra Films, where she is paid a monthly remuneration of ₹ 2 lakhs. She acts in various films produced by various producers. The remuneration for acting in such films is directly paid to Chopra Films by the different producers.

In this case, ₹ 2 lakhs will constitute salary in the hands of Sujata, since the relationship of employer and employee exists between Chopra Films and Sujata.

**Example 2:** In the above example, if Sujata acts in various films and gets fees from different producers, the same income will be chargeable as income from profession since the relationship of employer and employee does not exist between Sujata and the film producers.

**Example 3:** Commission received by a Director from a company is salary if the Director is an employee of the company. If, however, the Director is not an employee of the company, the said commission cannot be charged as salary but has to be charged either as income from business or as income from other sources depending upon the facts.

**Example 4:** *Salary paid to a partner by a firm is nothing but an appropriation of profits. 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. The same is to be charged as income from profits and gains of business or profession. This is primarily because the relationship between the firm and its partners is not that of an employer and employee.*

- (2) **Full-time or part-time employment:** Once the relationship of employer and employee exists, the income is to be charged under the head “salaries”. It does not matter whether the employee is a full-time employee or a part-time one.

If, for example, an employee works with more than one employer, salaries received from all the employers should be clubbed and brought to charge for the relevant previous years.

- (3) **Foregoing of salary:** Once salary accrues, the subsequent waiver by the employee does not absolve him from liability to income-tax. Such waiver is only an application and hence, chargeable to tax.

**Example 5:**

*Mr. X, an employee instructs his employer that he is not interested in receiving the salary for April 2021 and the same might be donated to a charitable institution.*

*In this case, Mr. X cannot claim that he cannot be charged in respect of the salary for April 2021. It is only due to his instruction that the donation was made to a charitable institution by his employer. It is only an application of income.*

*Hence, the salary for the month of April 2021 will be taxable in the hands of Mr. X. He is however, entitled to claim a deduction under section 80G for the amount donated to the institution. [The concept of deductions is explained in detail in Chapter 11: Deductions from Gross Total Income].*

- (4) **Surrender of salary:** However, if an employee surrenders his salary to the Central Government under section 2 of the Voluntary Surrender of Salaries (Exemption from Taxation) Act, 1961, the salary so surrendered would be exempt while computing his taxable income.
- (5) **Salary paid tax-free:** This, in other words, means that the employer bears the burden of the tax on the salary of the employee. In such a case, the income from salaries in the hands of the employee will consist of his salary income and also the tax on this salary paid by the employer.

However, as per section 10(10CC), the income-tax paid by the employer on non-monetary perquisites on behalf of the employee would be exempt in the hands of the employee.

- (6) **Place of accrual of salary:** Under section 9(1)(ii), salary earned in India is deemed to accrue or 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.

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

**Example 6:**

*Suppose, Mr. A, a citizen of India is posted in the United States as our Ambassador. Obviously, he renders his services outside India. He also receives his salary outside India. He is also a non-resident. The question, therefore, arises whether he can claim exemption in respect of his salary paid by the Government of India to him outside India.*

*Section 9(1)(iii) provides that salaries payable by the Government to a citizen of India for services outside India shall be deemed to accrue or arise in India. However, by virtue of section 10(7), any allowance or perquisites paid or allowed outside India by the Government to a citizen of India for rendering services outside India will be fully exempt.*

Now, let us discuss the chargeability under section 15, the provisions explaining the meaning of Salary, Perquisites and Profits in lieu of salary contained in section 17 and the deductions under section 16.



## 4.2 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.

**Example 7:** *If A draws his salary in advance for the month of April 2022 in the month of March 2022 itself, the same becomes chargeable on **receipt basis** and is to be assessed as income of the P.Y. 2021-22 i.e., A.Y. 2022-23. However, the salary for the A.Y. 2023-24 will not include that of April 2022.*

**Example 8:** *If the salary due for March 2022 is received by A later in the month of April 2022, it is still chargeable as income of the P.Y. 2021-22 i.e., A.Y. 2022-23 on **due basis**. Obviously, salary for the A.Y. 2023-24 will not include that of March 2022.*

### (1) Advance Salary

Advance salary is taxable when it is received by the employee irrespective of the fact whether it is due or not. It may so happen that when advance salary is included and charged in a particular

previous year, the rate of tax at which the employee is assessed may be higher than the normal rate of tax to which he would have been assessed. Section 89 provides for relief in these types of cases. The concept of relief under section 89 is explained in this Chapter later on.

### **Difference between advance salary and advance against salary**

Loan is different from salary. When an employee takes a loan from his employer, which is repayable in certain specified installments, the loan amount cannot be brought to tax as salary of the employee.

Similarly, advance against salary is different from advance salary. It is an advance taken by the employee from his employer. This advance is generally adjusted with his salary over a specified time period. It cannot be taxed as salary.

### **(2) Arrears of salary**

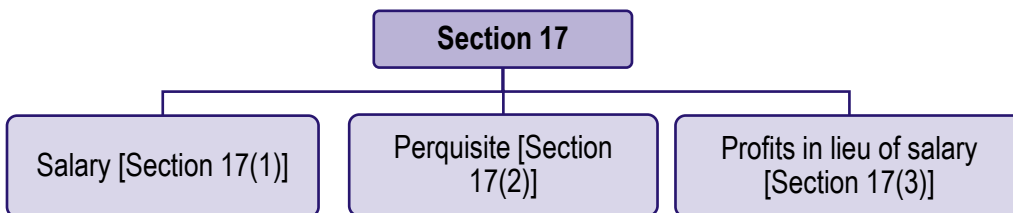
Normally speaking, salary arrears must be charged on due basis. However, there are circumstances when it may not be possible to bring the same to charge on due basis.

#### **Example 9:**

*If the Pay Commission is appointed by the Central Government and it recommends revision of salaries of employees with retrospective date, the arrears received in that connection will be charged on receipt basis. Here also, relief under section 89 is available.*



## **4.3 SALARY, PERQUISITE AND PROFITS IN LIEU OF SALARY (SECTION 17)**



### **(1) Meaning of Salary**

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:**

- (i) wages,
- (ii) any annuity or pension,
- (iii) any gratuity,
- (iv) any fees, commission, perquisite or profits in lieu of or in addition to any salary or wages,
- (v) any advance of salary,
- (vi) any payment received in respect of any period of leave not availed by him i.e. leave salary or leave encashment,
- (vii) **Provident Fund:**
  - the portion of the annual accretion in any previous year to the balance at the credit of an employee participating in a recognised provident fund to the extent it is taxable and
  - transferred balance in recognized provident fund to the extent it is taxable,
- (viii) 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.

**(i) Wages**

In common parlance, the term "wages" means fixed regular payment earned for work or services. The words "wages", "salary", "basic salary" are used interchangeably. Moreover, the payments in the form of Bonus, Allowances etc. made to the employee are also included within the meaning of salary.

Under the Income-tax Act, 1961, there are certain payments made which are fully taxable, partly taxable and fully exempt. For example, wages, salary, bonus, dearness allowance etc. are fully taxable payments. Whereas monetary benefits in the form of allowances such as House Rent Allowance, conveyance allowance etc. are partially taxable.

**Allowances**

Different types of allowances are given to employees by their employers. Generally, allowances are given to employees to meet some particular requirements like house rent, expenses on uniform, conveyance etc. Under the Income-tax Act, 1961, allowance is taxable on due or receipt basis, whichever is earlier. Various types of allowances normally in vogue are discussed below:

Allowances		
Fully Taxable	Partly Taxable	Fully Exempt
(i) Entertainment Allowance	(i) House Rent Allowance [u/s 10(13A)]	(i) Allowances to High Court Judges
(ii) Dearness Allowance	(ii) Special Allowances [u/s 10(14)]	(ii) Allowance paid by the United Nations Organization

Allowances		
Fully Taxable	Partly Taxable	Fully Exempt
(iii) Overtime Allowance (iv) Fixed Medical Allowance (v) City Compensatory Allowance (to meet increased cost of living in cities) (vi) Interim Allowance (vii) Servant Allowance (viii) Project Allowance (ix) Tiffin/Lunch/Dinner Allowance (x) Any other cash allowance (xi) Warden Allowance (xii) Non-practicing Allowance (xiii) Transport allowance to employee other than blind/ deaf and dumb/ orthopedically handicapped employee		(iii) Compensatory Allowance received by a judge (iv) Sumptuary allowance granted to High Court or Supreme Court Judges (v) Allowance granted to Government employees outside India.

#### (A) Allowances which are fully taxable

- (1) **City compensatory allowance:** City Compensatory Allowance is normally intended to compensate the employees for the higher cost of living in cities. It is taxable irrespective of the fact whether it is given as compensation for performing his duties in a particular place or under special circumstances.
- (2) **Entertainment allowance:** This allowance is given to employees to meet the expenses towards hospitality in receiving customers etc. The Act gives a deduction towards entertainment allowance only to a **Government employee**. The details of deduction permissible are discussed later on in this Chapter.
- (3) **Transport allowance:** Transport allowance granted to an employee to meet his expenditure for the purpose of commuting between the place of his residence and the place of his duty is fully taxable. However, in case of blind / deaf and dumb/ orthopedically handicapped employees, exemption upto ₹ 3,200 p.m. is provided under section 10(14)(ii) read with Rule 2BB.

**(B) Allowances which are partially taxable**

- (1) **House rent allowance [Section 10(13A)]:** HRA is a special allowance specifically granted to an employee by his employer towards payment of rent for residence of the employee. HRA granted to an employee is exempt to the extent of least of the following:

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

**Notes:**

- Exemption is not available to an assessee who lives in his own house, or in a house for which he has not incurred the expenditure of rent.
- “Salary” for this purpose means basic salary, dearness allowance, if provided in terms of employment, and commission as a fixed percentage of turnover.
- “Relevant period” means the period during which the said accommodation was occupied by the assessee during the previous year.

**ILLUSTRATION 1**

*Mr. Ramesh has the following receipts from his employer:*

(1) Basic pay	₹ 30,000 p.m.
(2) Dearness allowance (D.A.)	₹ 3,000 p.m.
(3) Commission	₹ 25,000 p.a.
(4) Motor car for personal use (expenditure met by the employer)	₹ 1,000 p.m.
(5) House rent allowance	₹ 12,000 p.m.

*Find out the amount of HRA eligible for exemption to Mr. Ramesh assuming that he paid a rent of ₹ 10,000 p.m. for his accommodation at Jaipur. DA forms part of salary for retirement benefits.*

**SOLUTION**

HRA received	₹ 1,44,000
Less: Exempt under section 10(13A) read with rule 2A [Working Note]	₹ 80,400
<b>Taxable HRA</b>	<b>₹ 63,600</b>



**Note:** Exemption shall be least of the following three limits:

- (a) the actual amount received ( $\text{₹ } 12,000 \times 12$ ) = ₹ 1,44,000
- (b) excess of the actual rent paid by the assessee over 10% of his salary  
 = Rent Paid - 10% of salary for the relevant period  
 = ( $\text{₹ } 10,000 \times 12$ ) - 10% of [ $\text{₹ } 30,000 + \text{₹ } 3,000$ ]  $\times 12$   
 = ₹ 1,20,000 - ₹ 39,600 = ₹ 80,400
- (c) 40% salary as his accommodation is situated at Jaipur  
 = 40% of [ $\text{₹ } 30,000 + \text{₹ } 3,000$ ]  $\times 12$  = ₹ 1,58,400

**Note:** For the purpose of exemption under section 10(13A), salary includes basic salary, dearness allowance, if provided in terms of employment, and commission as a fixed percentage of turnover, but excludes all other allowances and perquisites.

## ILLUSTRATION 2

Mr. Manoj is employed with RIL Ltd. on a basic salary of ₹ 15,000 p.m. He is also entitled to dearness allowance @100% of basic salary, 50% of which is included in salary as per terms of employment. The company gives him house rent allowance of ₹ 5,000 p.m. which was increased to ₹ 6,000 p.m. with effect from 1.01.2022. He also got an increment of ₹ 1,500 p.m. in his basic salary with effect from 1.02.2022. Rent paid by him during the previous year 2021-22 is as under:

- April and May, 2021 - Nil, as he stayed with his parents
- June to October, 2021 - ₹ 5,000 p.m. for an accommodation in Faridabad
- November, 2021 to March, 2022 - ₹ 7,000 p.m. for an accommodation in Delhi

Compute his gross salary for assessment year 2022-23 assuming he has not opted for the provisions of section 115BAC.

## SOLUTION

### Computation of gross salary of Mr. Manoj for A.Y. 2022-23

Particulars	₹
Basic salary [ $(\text{₹ } 15,000 \times 10) + (\text{₹ } 16,500 \times 2)$ ]	1,83,000
Dearness Allowance (100% of basic salary)	1,83,000
House Rent Allowance (See Note below)	25,950
<b>Gross Salary</b>	<b>3,91,950</b>

**Note: Computation of Taxable House Rent Allowance (HRA)**

Particulars	April-May (₹)	June-Oct (₹)	Nov-Dec (₹)	Jan (₹)	Feb-March (₹)
Basic salary per month	15,000	15,000	15,000	15,000	16,500
Dearness allowance (included in salary as per terms of employment) (50% of basic salary)	7,500	7,500	7,500	7,500	8,250
Salary per month for the purpose of computation of house rent allowance exemption	22,500	22,500	22,500	22,500	24,750
<b>Relevant period (in months)</b>	<b>2</b>	<b>5</b>	<b>2</b>	<b>1</b>	<b>2</b>
Salary for the relevant period (Salary per month × relevant period)	45,000	1,12,500	45,000	22,500	49,500
Rent paid for the relevant period	Nil	25,000 (₹5,000×5)	14,000 (₹7,000×2)	7,000 (₹7,000×1)	14,000 (₹7,000×2)
House rent allowance (HRA) received during the relevant period <b>(A)</b>	10,000 (₹5,000×2)	25,000 (₹5,000×5)	10,000 (₹5,000×2)	6,000 (₹6,000×1)	12,000 (₹6,000×2)
Least of the following is exempt [u/s 10(13A)]	N.A.				
1. Actual HRA received	-	25,000	10,000	6,000	12,000
2. Rent paid – 10% of salary	-	13,750	9,500	4,750	9,050
3. 40% of salary (Residence at Faridabad – June to Oct, 2021)	-	45,000 (40% × ₹ 1,12,500)	22,500 (50% × ₹ 45,000)	11,250 (50% × ₹ 22,500)	24,750 (50% × ₹ 49,500)
50% of salary (Residence at Delhi – Nov, 2021- March, 2022)					
<b>Exempt HRA (B)</b>	<b>Nil</b>	<b>13,750</b>	<b>9,500</b>	<b>4,750</b>	<b>9,050</b>
Taxable HRA (Actual HRA – Exempt HRA) <b>(A-B)</b>	10,000	11,250	500	1,250	2,950

Taxable HRA (total) = ₹ 10,000 + ₹ 11,250 + ₹ 500 + ₹ 1,250 + ₹ 2,950 = ₹ 25,950

(2) **Special allowances to meet expenses relating to duties or personal expenses [Section 10(14)]:** This clause provides for exemption (as per Rule 2BB) in respect of the following:

- (i) Special allowances or benefit not being in the nature of a perquisite, specifically granted to meet expenses incurred wholly, necessarily and exclusively in the performance of the duties of an office or employment of profit **[Section 10(14)(i)]**

For the allowances under this category, **there is no limit on the amount which the employee can receive from the employer**, but whatever amount is received should be fully utilized for the purpose for which it was given to him.

- (ii) Special allowances granted to the assessee either to meet his personal expenses at the place where the duties of his office or employment of profit are ordinarily performed by him or at the place where he ordinarily resides or to compensate him for the increased cost of living. **[Section 10(14)(ii)]**

For the allowances under this category, **there is a limit on the amount which the employee can receive from the employer**. Any amount received by the employee in excess of these specified limits will be taxable in his hands as income from salary for the year. It does not matter whether the amount which is received is actually spent or not by the employee for the purpose for which it was given to him.

**Rule 2BB**

The following allowances have been prescribed in Rule 2BB:

**Allowances prescribed for the purposes of section 10(14)(i) [Rule 2BB(1)]**

- (a) any allowance granted to meet the cost of travel on tour or on transfer (**Travelling Allowance**);

**Explanation** – “allowance granted to meet the cost of travel on transfer” includes any sum paid in connection with the transfer, packing and transportation of personal effects on such transfer.

- (b) 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 (**Daily allowance/Per-diem allowance**);

- (c) any allowance granted to meet the expenditure incurred on conveyance in performance of duties of an office or employment of profit (**Conveyance Allowance**);

Such allowance would be exempt only if free conveyance is not provided by the employer.

- (d) any allowance granted to meet the expenditure incurred on a helper where such helper is engaged in the performance of the duties of an office or employment of profit (**Helper Allowance**);

- (e) any allowance granted for encouraging the academic research and training pursuits in educational and research institutions (**Research allowance**);
- (f) any allowance granted to meet the expenditure on the purchase or maintenance of uniform for wear during the performance of the duties of an office or employment of profit (**Uniform Allowance**).

**Note** - An employee, being an assessee, who opts for the provisions of section 115BAC would be entitled for exemption only in respect of travelling allowance, daily allowance and conveyance allowance mentioned in (a) to (c) above.

**Allowances prescribed for the purposes of section 10(14)(ii) [Rule 2BB(2)]**

S. No.	Name of Allowance	Extent to which allowance is exempt
1.	Any Special Compensatory Allowance in the nature of <b>Special Compensatory (Hilly Areas) Allowance</b> or High Altitude Allowance or Uncongenial Climate Allowance or Snow Bound Area Allowance or Avalanche Allowance	₹ 800 or ₹ 300 per month depending upon the specified locations ₹ 7,000 per month in Siachen area of Jammu and Kashmir
2.	Any Special Compensatory Allowance in the nature of <b>border area allowance or remote locality allowance or difficult area allowance or disturbed area allowance</b>	₹ 1,300 or ₹ 1,100 or ₹ 1,050 or ₹ 750 or ₹ 300 or ₹ 200 per month depending upon the specified locations
3.	<b>Special Compensatory (Tribal Areas / Schedule Areas / Agency Areas) Allowance [Specified States]</b>	₹ 200 per month
4.	Any allowance granted to an employee <b>working in any transport system</b> to meet his personal expenditure during his duty performed in the course of running such transport from one place to another, provided that such employee is not in receipt of daily allowance	70% of such allowance upto a maximum of ₹ 10,000 per month
5.	<b>Children Education Allowance</b>	₹ 100 per month per child upto a maximum of two children
6.	Any allowance granted to an employee to meet the <b>hostel expenditure</b> on his child	₹ 300 per month per child upto a maximum of two children
7.	<b>Compensatory Field Area Allowance [Specified areas in Specified States]</b>	₹ 2,600 per month
8.	<b>Compensatory Modified Field Area Allowance [Specified areas in Specified States]</b>	₹ 1,000 per month

9.	Any <b>special allowance</b> in the nature of counter <b>insurgency allowance granted to the members of the armed forces</b> operating in areas away from their permanent locations.	₹ 3,900 per month
10.	Any <b>transport allowance</b> granted to an employee who is blind <b>or deaf and dumb</b> or orthopedically handicapped with disability of the lower extremities of the body, to meet his expenditure for commuting between his residence and place of duty	₹ 3,200 per month.
11.	<b>Underground Allowance</b> granted to an employee who is working in uncongenial, unnatural climate in underground mines.	₹ 800 per month
12.	Any special allowance in the nature of <b>high Altitude allowance</b> granted to the member of the armed forces operating in high altitude areas For altitude of 9,000 to 15,000 feet For above 15,000 feet	₹ 1,060 per month ₹ 1,600 per month
13.	Any special allowance in the nature of <b>special compensatory highly active field area allowance</b> granted to the member of the armed forces	₹ 4,200 per month
14.	Any special allowance in the nature of <b>Island (duty) allowance</b> granted to the member of the armed forces in <b>Andaman &amp; Nicobar and Lakshadweep Group of Islands</b>	₹ 3,250 per month

**Notes:**

- (i) Any assessee claiming exemption in respect of allowances mentioned at serial numbers 7 & 8 and 9 shall not be entitled to exemption in respect of the allowance and disturbed area allowance referred at serial number 2, respectively.
- (ii) An employee, being an assessee, who opts for the provisions of section 115BAC would be entitled for exemption only in respect of transport allowance granted to an employee who is blind or deaf and dumb or orthopedically handicapped with disability of the lower extremities of the body to the extent of ₹ 3,200 p.m.

**ILLUSTRATION 3**

Mr. Shashank has two sons. He is in receipt of children education allowance of ₹ 250 p.m. for his elder son and ₹ 80 p.m. for his younger son. Both his sons are going to school. He also receives the following allowances:

Transport allowance : ₹ 1,900 p.m.

Special compensatory tribal area allowance for his posting in Bihar : ₹ 800 p.m.

Compute his taxable allowances.

**SOLUTION**

Taxable allowance in the hands of Mr. Shashank is computed as under -

Children Education Allowance:

Elder son  $[(₹250 - ₹100) \text{ p.m.} \times 12 \text{ months}] = ₹ 1,800$

Younger son  $[(₹ 80 - ₹ 80) \text{ p.m.} \times 12 \text{ months}] = \underline{\text{Nil}} \quad ₹ 1,800$

Transport allowance  $(₹1,900 \times 12 \text{ months}) \quad ₹ 22,800$

Tribal area allowance  $[(₹800 - ₹200) \text{ p.m.} \times 12 \text{ months}] \quad ₹ 7,200$

**Taxable allowances** **₹ 31,800**

**Note:** Transport allowance is exempt to the extent of ₹ 3200 per month only in case of an employee who is blind or deaf and dumb or orthopaedically handicapped with disability of lower extremities.

**ILLUSTRATION 4**

Ayush, an employee of a management consultancy firm, was sent to UK in connection with a project of the firm's client for two months in the previous year. In addition to his salary, the firm paid per diem allowance for the period when he worked in UK to meet expenses on boarding and lodging. Tax was not deducted at source from such allowance by the employer. Ayush did not include such allowance in computation of his taxable salary for the relevant assessment year. In course of assessment of Ayush under section 143(3), the Assessing Officer sent a notice to him asking him to explain why the per diem allowance received by him should not be charged to tax? Ayush has sought your advice.

**SOLUTION**

Per-diem allowance is exempt from tax under section 10(14)(i) read with Rule 2BB, as it is an allowance granted and spent to meet the ordinary daily charges incurred by an employee on account of absence from his normal place of duty. Rule 2BB exempts the allowance granted to meet the ordinary daily charges incurred by an employee on account of his absence from his normal place of duty.

In the given case, Mr. Ayush was posted for a period of 2 months outside his normal place of duty and the allowance was paid to meet the boarding and lodging.

Therefore, the allowance would fall under section 10(14)(i) read with Rule 2BB and would hence be exempt, assuming that the expenditure to that extent was actually incurred by him towards his boarding and lodging.

### (C) Allowances which are fully exempt

- (1) **Allowance to Supreme Court/ High Court Judges:** Any allowance paid to a Judge of a High Court and Supreme Court under section 22A(2) of the High Court Judges (Conditions of Service) Act, 1954 and section 23(1A) of the Supreme Court Judges (Salaries and Conditions of services) Act, 1958, respectively, is not taxable.
- (2) **Allowance paid by the United Nations Organisation (UNO):** Allowance paid by the UNO to its employees is not taxable by virtue of section 2 of the United Nations (Privileges and Immunities) Act, 1947.
- (3) **Compensatory allowance under section 222(2) of the Constitution:** Compensatory allowance received by judge under Article 222(2) of the Constitution is not taxable since it is neither salary nor perquisite — *Bishamber Dayalv. CIT [1976] 103 ITR 813 (MP)*.
- (4) **Sumptuary allowance:** Sumptuary allowance given to High Court Judges under section 22C of the High Court Judges (Conditions of Service) Act, 1954 and Supreme Court Judges under section 23B of the Supreme Court Judges (Conditions of Service) Act, 1958 is not chargeable to tax.
- (5) **Allowances payable outside India [Section 10(7)]:** Allowances or perquisites paid or allowed as such outside India by the Government to a citizen of India for services rendered outside India are exempt from tax.

Students may remember that in such cases under section 9(1)(iii), the income chargeable under the head 'Salaries' is deemed to accrue in India. The residential status of the recipient will, however, not affect this exemption.

### (ii) Annuity or Pension

#### Meaning of Annuity

- As per the definition, 'annuity' is treated as salary. Annuity is a sum payable in respect of a particular year. It is a yearly grant. If a person invests some money entitling him to series of equal annual sums, such annual sums are annuities in the hands of the investor.
- Annuity received from a present employer is to be taxed as salary. It does not matter whether it is paid in pursuance of a contractual obligation or voluntarily.
- Annuity received from a past employer is taxable as profit in lieu of salary.
- Annuity received from person other than an employer is taxable as "Income from other sources".

## Pension

*Concise Oxford Dictionary* defines 'pension' as a periodic payment made especially by Government or a company or other employers to the employee in consideration of past service payable after his retirement.

Pension is of two types: commuted and uncommuted.

- **Uncommuted Pension:** Uncommuted pension refers to pension received periodically. It is fully taxable in the hands of both government and non-government employees.
- **Commuted Pension:** Commutation means inter-change. Commuted pension means lump sum amount taken by commuting the whole or part of the pension. Many persons convert their future right to receive pension into a lumpsum amount receivable immediately.

### **Example 10:**

*Suppose a person is entitled to receive a pension of say ₹ 20,000 p.m. for the rest of his life. He may commute ¼th i.e., 25% of this amount and get a lumpsum of say ₹ 3,00,000. After commutation, his pension will now be the balance 75% of ₹ 20,000 p.m. = ₹ 15,000 p.m.*

### **Exemption in respect of Commuted Pension [Section 10(10A)]**

As per section 10(10A), the payment in respect of commuted pension is exempt, subject to the conditions specified therein. Its treatment is discussed below:

- Employees of the Central Government/ local authorities/ Statutory Corporation/ members of the Civil Services/ Defence Services:** Any commuted pension received is fully exempt from tax.
- Other Employees:** Any commuted pension received is exempt from tax in the following manner:

#### **If the employee is in receipt of gratuity also.**

Exemption =  $\frac{1}{3}$ <sup>rd</sup> of the amount of pension which he would have received had he commuted the whole of the pension.

$$= \left[ \frac{1}{3} \times \frac{\text{Commuted Pension Received}}{\text{Commutation \%}} \times 100\% \right]$$

#### **If the employee does not receive any gratuity**

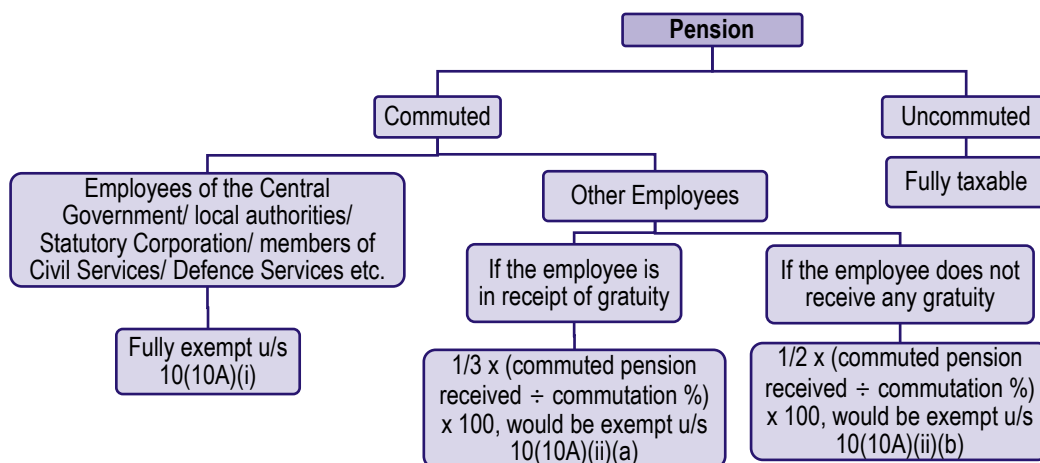
Exemption =  $\frac{1}{2}$  of the amount of pension which he would have received had he commuted the whole of the pension.

$$= \left[ \frac{1}{2} \times \frac{\text{Commuted Pension Received}}{\text{Commutation \%}} \times 100\% \right]$$



**Notes:**

1. Judges of the Supreme Court and High Court will be entitled to exemption of the commuted portion.
2. Any commuted pension received by an individual out of annuity plan of the Life Insurance Corporation of India (LIC) from a fund set up by that Corporation will be exempted.

**ILLUSTRATION 5**

Mr. Akash retired on 1.11.2021 receiving ₹ 10,000 p.m. as pension. On 1.1.2022, he commuted 50% of his pension and received ₹ 5,00,000 as commuted pension. You are required to compute his taxable pension assuming:

- (a) He is a government employee.
- (b) He is a private sector employee, receiving gratuity of ₹ 7,00,000 at the time of retirement.
- (c) He is a private sector employee and is not in receipt of gratuity at the time of retirement.

**SOLUTION****(a) He is a government employee**

Uncommuted pension received (November – March)		₹ 35,000
[(₹ 10,000 × 2 months) + (50% of ₹ 10,000 × 3 months)]		
Commuted pension received	₹ 5,00,000	
Less: Exempt u/s 10(10A)(i)	₹ 5,00,000	<u>NIL</u>
<b>Taxable pension</b>		<u><b>₹ 35,000</b></u>

**(b) He is a private sector employee, receiving gratuity ₹ 7,00,000 at the time of retirement**

Uncommuted pension received (November – March) ₹ 35,000

[(₹ 10,000 × 2 months) + (50% of ₹ 10,000 × 3 months)]

Commuted pension received ₹ 5,00,000

Less: Exempt u/s 10(10A)(ii)(a)

$$\left[ \frac{1}{3} \times \frac{5,00,000}{50\%} \times 100\% \right] \quad \text{₹ } \underline{3,33,333} \quad \text{₹ } \underline{1,66,667}$$

**Taxable pension** ₹ 2,01,667

**(c) He is a private sector employee and is not in receipt of gratuity at the time of retirement**

Uncommuted pension received (November – March) ₹ 35,000

[(₹ 10,000 × 2 months) + (50% of ₹ 10,000 × 3 months)]

Commuted pension received ₹ 5,00,000

Less: Exempt u/s 10(10A)(ii)(b)

$$\left[ \frac{1}{2} \times \frac{5,00,000}{50\%} \times 100\% \right] \quad \text{₹ } \underline{5,00,000} \quad \text{NIL}$$

**Taxable pension** ₹ 35,000

**(iii) Gratuity**

Gratuity is a voluntary payment made by an employer in appreciation of services rendered by the employee. Now-a-days, gratuity has become a normal payment applicable to all employees. In fact, the Payment of Gratuity Act, 1972 is a statutory recognition of the concept of gratuity. Almost all employers enter into an agreement with employees to pay gratuity.

**Exemption in respect of Gratuity [Section 10(10)]**

Its treatment is discussed below:

1. Retirement gratuity received under the Pension Code Regulations applicable to members of the Defence Service is fully exempt from tax.
2. **Employees of Central Government/ Members of Civil Services/ local authority employees:** Any death cum retirement gratuity is fully exempt from tax under section 10(10)(i).

### 3. Other employees:

#### (i) Covered by the Payment of Gratuity Act, 1972

Any death-cum-retirement gratuity is exempt from tax to the extent of least of the following:

- (a) ₹ 20,00,000
- (b) Gratuity actually received
- (c) 15 days' salary based on last drawn salary for each completed year of service or part thereof in excess of 6 months

**Note:** Salary for this purpose means basic salary and dearness allowance. No. of days in a month for this purpose, shall be taken as 26.

#### (ii) Not covered by the Payment of Gratuity Act, 1972

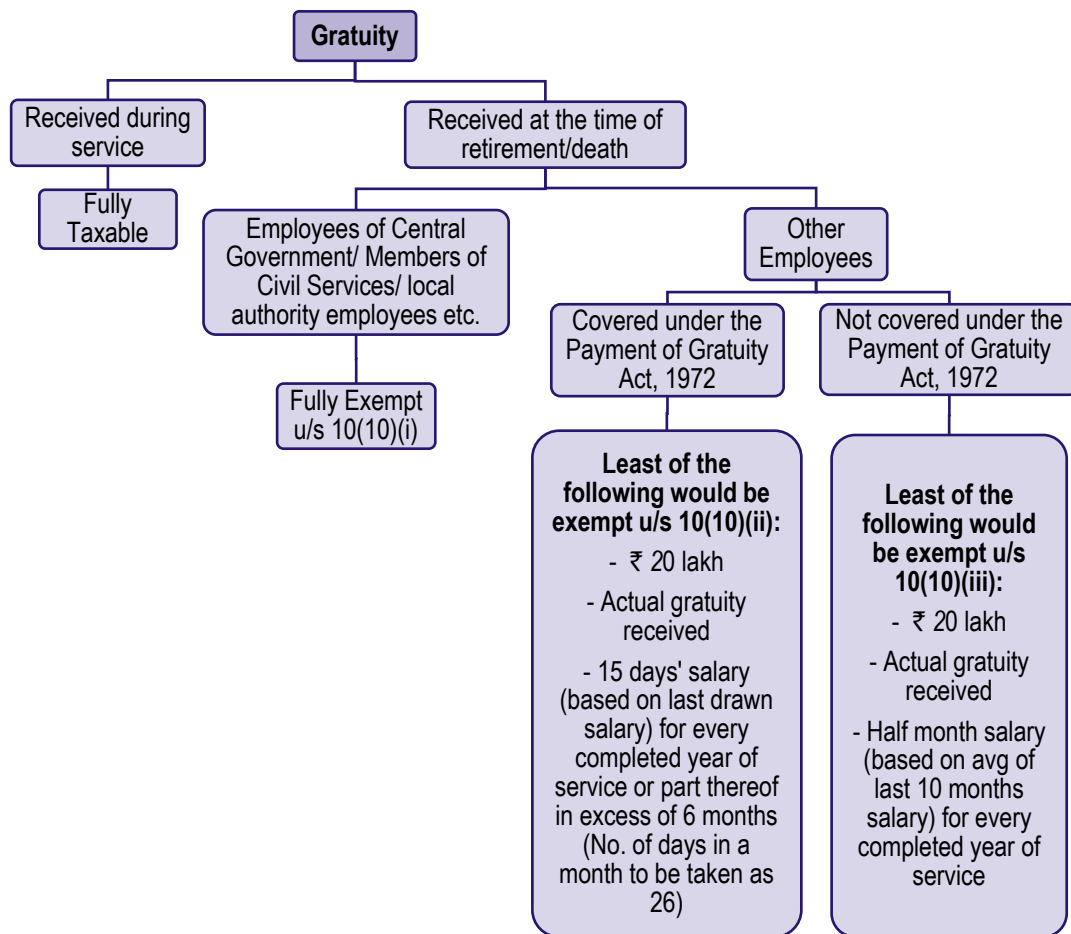
Any death cum retirement gratuity received by an employee on his retirement or his becoming incapacitated prior to such retirement or on his termination or any gratuity received by his widow, children or dependents on his death is exempt from tax to the extent of least of the following:

- (a) ₹ 20,00,000
- (b) Gratuity actually received
- (c) Half month's salary (based on last 10 months' average salary immediately preceding the month of retirement or death) for each completed year of service (fraction to be ignored)

**Note:** Salary for this purpose means basic salary and dearness allowance, if provided in the terms of employment for retirement benefits, forming part of salary and commission which is expressed as a fixed percentage of turnover.

***Students must also note the following points:***

- (1) *Gratuity received during the period of service is fully taxable.*
- (2) *Where gratuity is received from 2 or more employers in the same year then aggregate amount of gratuity exempt from tax cannot exceed ₹ 20,00,000.*
- (3) *Where gratuity is received in any earlier year from former employer and again received from another employer in a later year, the limit of ₹ 20,00,000 will be reduced by the amount of gratuity exempt earlier.*



#### ILLUSTRATION 6

Mr. Harish retired on 15.7.2021 after completion of 26 years 8 months of service and received gratuity of ₹ 12,00,000. At the time of retirement, his salary was:

Basic Salary : ₹ 40,000 p.m.

Dearness Allowance : ₹ 10,000 p.m. (70% of which is for retirement benefits)

Commission : 1% of turnover (turnover in the last 12 months was ₹ 1,50,00,000)

Bonus : ₹ 20,000 p.a.

Compute his taxable gratuity assuming:

- He is private sector employee and covered by the Payment of Gratuity Act 1972.
- He is private sector employee and not covered by the Payment of Gratuity Act 1972.
- He is a Government employee.

**SOLUTION****(a) He is covered by the Payment of Gratuity Act 1972**

Gratuity received at the time of retirement ₹ 12,00,000

Less: Exemption under section 10(10)(ii)

Least of the following:

i. Gratuity received ₹ 12,00,000

ii. Statutory limit ₹ 20,00,000

iii. 15 days' salary based on last drawn salary for each completed year of service or part thereof in excess of 6 months

$$\frac{15}{26} \times \text{last drawn salary} \times \text{years of service}$$

$$\frac{15}{26} \times (40,000 + 10,000) \times 27 = \text{₹ } 7,78,846 \quad \text{₹ } 7,78,846$$

**Taxable Gratuity** ₹ 4,21,154

**(b) He is not covered by the Payment of Gratuity Act 1972**

Gratuity received at the time of retirement ₹ 12,00,000

Less: Exemption under section 10(10)(iii) (**Note**) ₹ 7,73,500

**Taxable Gratuity** ₹ 4,26,500

**Note:** Exemption under section 10(10) is least of the following:

(i) Gratuity received ₹ 12,00,000

(ii) Statutory limit ₹ 20,00,000

(iii) Half month's salary based on average salary of last 10 months preceding the month of retirement for each completed year of service.

$$\text{i.e. } \frac{1}{2} \times \text{Average salary} \times \text{years of service}$$

$$= \frac{1}{2} \times \frac{[(40,000 \times 10) + (10,000 \times 70\% \times 10) + (1\% \times 1,50,00,000 \times \frac{10}{12})]}{10} \times 26$$

$$= \text{₹ } 7,73,500$$

**(c) He is a government employee**

Gratuity received at the time of retirement	₹ 12,00,000
Less: Exemption under section 10(10)(i)	<u>₹ 12,00,000</u>
<b>Taxable gratuity</b>	<u><b>Nil</b></u>

**(iv) Fees, commission, perquisites or profits in lieu of or in addition to any salary or wages**

Payment in the form of fees or commission by the employer to the employee are fully taxable. Commission may be paid as fixed percentage of turnover or net profits etc.

Section 17(2) and 17(3) contains the provisions relating to perquisites and profits in lieu of salary, respectively. The provisions of these sections would be discussed in detail separately in this Chapter.

**(v) Any Advance of Salary**

The concept of “Advance Salary” already discussed in this chapter.

**(vi) Leave Salary or Leave Encashment**

Generally, employees are allowed leaves during the period of service. Employee may avail such leave or in case the leave is not availed, then the leaves may either lapse or be accumulated for future or allowed to be encashed every year or at the time termination/ retirement. The payment received on account of encashment of unavailed leave would be form part of salary. However, section 10(10AA) provides exemption in respect of amount received by way of encashment of unutilised earned leave by an employee at the time of his retirement whether on superannuation or otherwise.

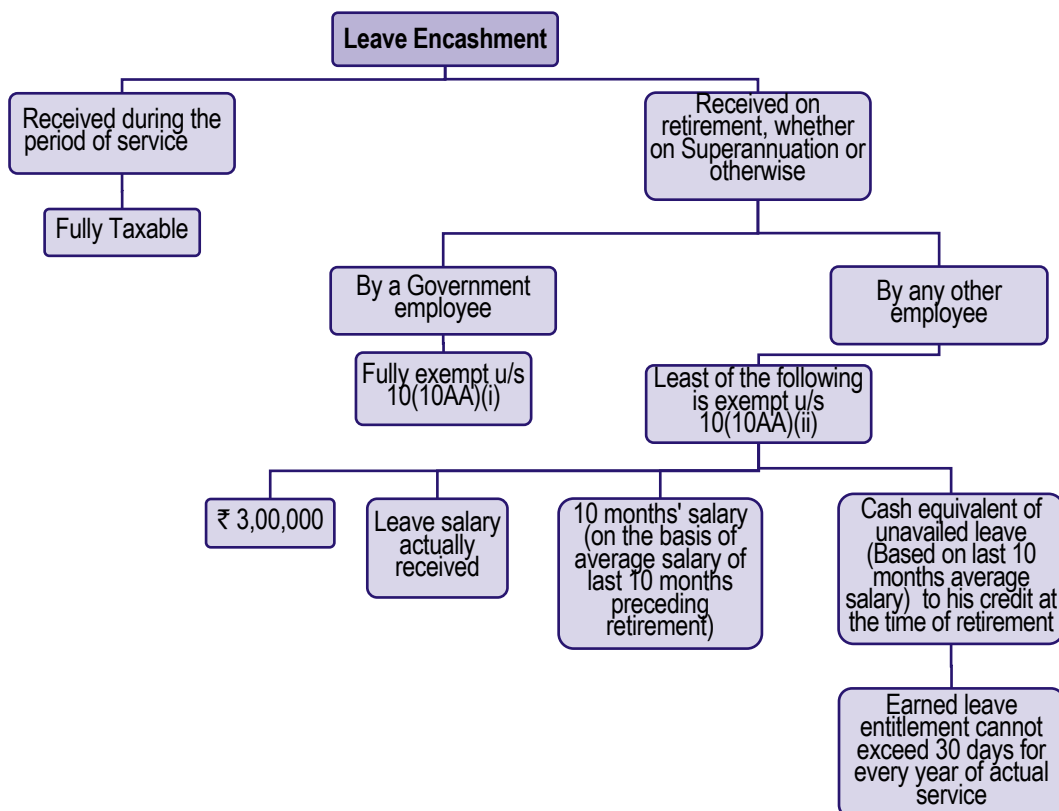
**Exemption of amount received by way of encashment of unutilised earned leave on retirement [Section 10(10AA)]**

The provisions of this clause are mentioned below:

- (a) Government employees:** Leave salary received at the time of retirement is fully exempt from tax.
- (b) Non-government employees:** Leave salary received at the time of retirement is exempt from tax to the extent of least of the following:
  - (i) ₹ 3,00,000
  - (ii) Leave salary actually received
  - (iii) 10 months' salary (on the basis of average salary of last 10 months )
  - (iv) Cash equivalent of leave (based on last 10 months' average salary immediately preceding the date of retirement) to the credit of the employee at the time of retirement or death. Earned leave entitlement cannot exceed 30 days for every year of actual service rendered for the employer from whose service he has retired.

**Notes:**

1. Leave salary received during the period of service is fully taxable.
2. Where leave salary is received from two or more employers in the same previous year, then, the aggregate amount of leave salary exempt from tax cannot exceed ₹ 3,00,000.
3. Where leave salary is received in any earlier previous year from a former employer and again received from another employer in a later year, the limit of ₹ 3,00,000 will be reduced by the amount of leave salary exempt earlier.
4. Salary for this purpose means basic salary and dearness allowance, if provided in the terms of employment for retirement benefits, and commission which is expressed as a fixed percentage of turnover.
5. 'Average salary' will be determined on the basis of the salary drawn during the period of ten months immediately preceding the date of his retirement whether on superannuation or otherwise.



**ILLUSTRATION 7**

Mr. Aggarwal retired on 1.12.2021 after 20 years of service, receiving leave salary of ₹ 10,00,000. Other details of his salary income are:

Basic Salary : ₹ 10,000 p.m. (₹ 2,000 was increased w.e.f. 1.4.2021)

Dearness Allowance : ₹ 6,000 p.m. (60% of which is for retirement benefits)

Commission : ₹ 1,000 p.m.

Bonus : ₹ 2,000 p.m.

Leave availed during service : 480 days

He was entitled to 30 days leave every year.

You are required to compute his taxable leave salary assuming:

- (a) He is a government employee.  
(b) He is a non-government employee.

**SOLUTION****(a) He is a government employee**

Leave Salary received at the time of retirement	₹ 10,00,000
Less: Exemption under section 10(10AA)(i)	<u>₹ 10,00,000</u>
<b>Taxable Leave salary</b>	<u><b>Nil</b></u>

**(b) He is a non-government employee**

Leave Salary received at the time of retirement	₹ 10,00,000
Less: Exempt under section 10(10AA)(ii) [See Note below]	<u>₹ 52,800</u>
<b>Taxable Leave Salary</b>	<u><b>₹ 9,47,200</b></u>

**Note:** Exemption under section 10(10AA)(ii) is least of the following:

- (i) Leave salary received ₹ 10,00,000  
(ii) Statutory limit ₹ 3,00,000  
(iii) 10 months' salary based on average salary of last 10 months

$$\begin{aligned} \text{i.e. } & \left[ 10 \times \frac{\text{Salary of last 10 months i.e. Feb - Nov}}{10 \text{ months}} \right] \\ & = \left[ 10 \times \frac{(10000 \times 8) + (8000 \times 2) + (60\% \times 6000 \times 10)}{10 \text{ months}} \right] \quad ₹ 1,32,000 \end{aligned}$$



- (iv) Cash equivalent of leave standing at the credit of the employee based on the average salary of last 10 months (max. 30 days per year of service)

Leave Due = Leave allowed – Leave taken

= (30 days per year × 20 years) – 480 days

= 120 days

$$\begin{aligned} \text{i.e. } & \left[ \frac{\text{Leave due (in days)}}{30 \text{ days}} \times \text{Average salary p.m.} \right] \\ & = \left[ \frac{120 \text{ days}}{30 \text{ days}} \times \frac{1,32,000}{10} \right] \quad \quad \quad \text{₹ 52,800} \end{aligned}$$

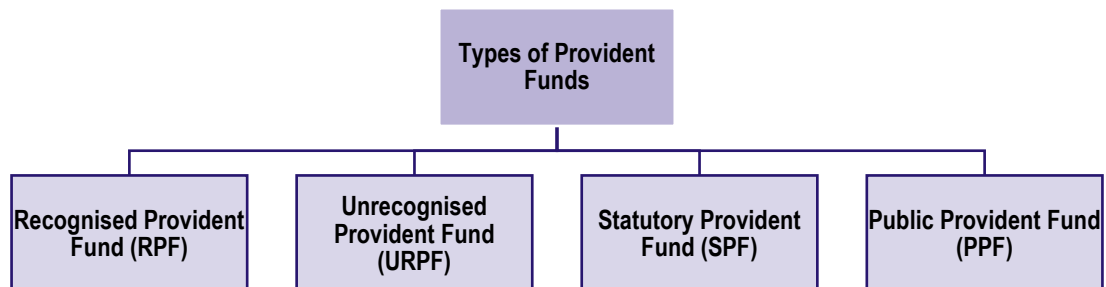
### (vii) *Provident fund*

Provident fund scheme is a scheme intended to give substantial benefits to an employee at the time of his retirement. Under this scheme, a specified sum is deducted from the salary of the employee as his contribution towards the fund. The employer also generally contributes the same amount out of his pocket, to the fund. The contributions of the employer and the employee are invested in approved securities. Interest earned thereon is also credited to the account of the employee. Thus, the credit balance in a provident fund account of an employee consists of the following:

- (i) employee's contribution
- (ii) interest on employee's contribution
- (iii) employer's contribution
- (iv) interest on employer's contribution.

The accumulated balance is paid to the employee at the time of his retirement or resignation. In the case of death of the employee, the same is paid to his legal heirs.

The provident fund represents an important source of small savings available to the Government. Hence, the Income-tax Act, 1961 gives certain deductions on savings in a provident fund account.



**(1) Recognised Provident Fund (RPF)**

Recognised provident fund means a provident fund recognised by the Commissioner of Income-tax for the purposes of income-tax. It is governed by Part A of Schedule IV to the Income-tax Act, 1961. This schedule contains various rules regarding the following:

- (a) Recognition of the fund
- (b) Employee's and employer's contribution to the fund
- (c) Treatment of accumulated balance etc.

A fund constituted under the Employees' Provident Fund and Miscellaneous Provisions Act, 1952 will also be a Recognised Provident Fund.

**(2) Unrecognised Provident Fund (URPF)**

A fund not recognised by the Commissioner of Income-tax is Unrecognised Provident Fund.

**(3) Statutory Provident Fund (SPF)**

The SPF is governed by Provident Funds Act, 1925. It applies to employees of government, railways, semi-government institutions, local bodies, universities and all recognised educational institutions.

**(4) Public Provident Fund (PPF)**

Public provident fund is operated under the Public Provident Fund Act, 1968. A membership of the fund is open to every individual though it is ideally suited to self-employed people. A salaried employee may also contribute to PPF in addition to the fund operated by his employer. An individual may contribute to the fund on his own behalf as also on behalf of a minor of whom he is the guardian.

For getting a deduction under section 80C, a member is required to contribute to the PPF a minimum of ₹ 500 in a year. The maximum amount that may qualify for deduction on this account is ₹ 1,50,000 as per PPF rules.

A member of PPF may deposit his contribution in as many installments in multiples of ₹ 500 as is convenient to him. The amount of contribution may be paid at any of the offices or branch offices of the State Bank of India or its subsidiaries and specified branches of banks or any Post Office.

**The tax treatment is given below:**

Particulars	Recognized PF	Unrecognized PF	Statutory PF	Public PF
<b>Employer's Contribution</b>	Contribution in excess of 12% of salary is taxable as "salary" u/s 17(1)	Not taxable at the time of contribution	Fully exempt	N.A. (as there is only assessee's own contribution)
<b>Employee's Contribution</b>	Eligible for deduction u/s 80C	Not eligible for deduction	Eligible for deduction u/s 80C	Eligible for deduction u/s 80C

<b>Interest Credited on Employer's Contribution</b>	Amount in excess of 9.5% p.a. is taxable as "salary" u/s 17(1)	Not taxable at the time of credit of interest	Fully exempt	N.A.
<b>Interest Credited on Employee's Contribution</b>	Amount in excess of 9.5% p.a. is taxable as "salary" u/s 17(1) [See Note below]	Not taxable at the time of credit of interest	Exempt upto certain limit of contribution [See Note below]	Fully exempt
<b>Amount withdrawn on retirement/termination</b>	Exempt u/s 10(12) subject to certain conditions detailed in the chart below	<ul style="list-style-type: none"> <li>Employee's contribution is not taxable.</li> <li>Interest on Employee's contribution is taxable under 'Income from Other Sources'.</li> <li>Employer's contribution and interest thereon is taxable as "Profit in lieu of salary" u/s 17(3).</li> </ul>	Exempt u/s 10(11)	Fully exempt u/s 10(11)

Salary for this purpose means basic salary and dearness allowance - if provided in the terms of employment for retirement benefits and commission as a percentage of turnover.

**Note - Interest credited on contribution by such person/employee**

*As per section 10(11), any payment from a Provident Fund (PF) to which Provident Fund Act, 1925, applies or from Public Provident Fund would be exempt.*

*Accumulated balance due and becoming payable to an employee participating in a Recognized Provident Fund (RPF) would be exempt under section 10(12).*

*However, the exemption under section 10(11) or 10(12) would not be available in respect of income by way of interest accrued during the previous year to the extent it relates to the amount or the aggregate of amounts of contribution made by that person/employee exceeding ₹ 2,50,000 in any previous year in that fund, on or after 1<sup>st</sup> April, 2021 and computed in prescribed manner.*

*If the contribution by such person/employee is in a fund in which there is no employer's contribution, then, a higher limit of ₹ 5,00,000 would be applicable for such contribution, and interest accrued in any previous year in that fund, on or after 1<sup>st</sup> April, 2021 would be exempt upto that limit.*

*It may be noted that interest accrued on contribution to such funds upto 31<sup>st</sup> March, 2021 would be exempt without any limit, even if the accrual of income is after that date.*

*The CBDT has, vide Rule 9D, notified the manner to calculate taxable interest relating to contribution in a provident fund or recognized provident fund, exceeding threshold limit.*

*Interest income accrued during the previous year which is not exempt from inclusion in the total income of a person (taxable interest) shall be computed as the interest accrued during the previous year in the taxable contribution account.*

*For this purpose, separate accounts within the provident fund account shall be maintained during the previous year 2021-22 and all subsequent previous years for taxable contribution and non-taxable contribution made by a person.*

*(a) Non-taxable contribution account – Aggregate of*

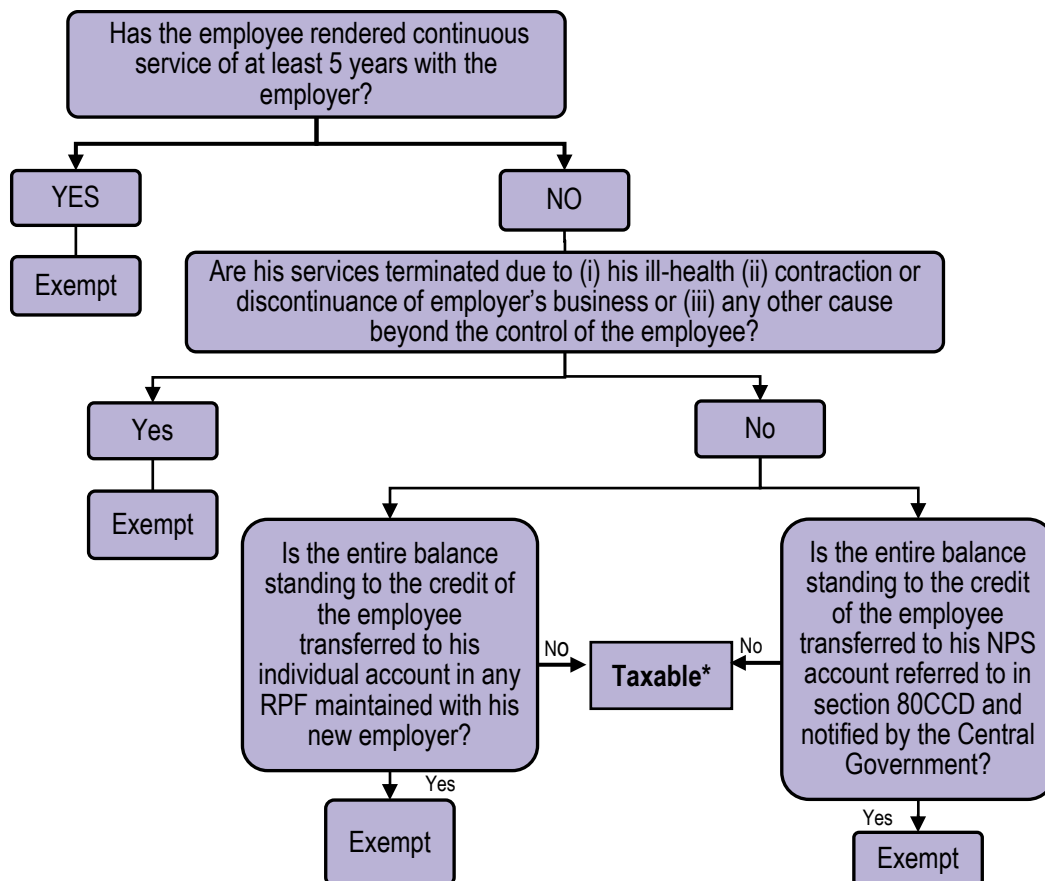
- (i) closing balance in the account as on 31.03.2021;*
  - (ii) any contribution made by the person in the account during the previous year 2021-22 and subsequent previous years, which is not included in the taxable contribution account; and*
  - (iii) interest accrued on (i) and (ii),*
- as reduced by the withdrawal, if any, from such account.*

*(b) Taxable contribution account – Aggregate of*

- (i) contribution made by the person in the account during the previous year 2021-22 and subsequent previous years, which is in excess of the yearly threshold limit; and*
  - (ii) interest accrued on (i)*
- as reduced by the withdrawal, if any, from such account.*

*Yearly threshold limit is ₹ 5,00,000, if the contribution by such person/employee is in a fund in which there is no employer's contribution and ₹ 2,50,000 in other cases.*

### Exemption of Accumulated balance of RPF, payable to an employee



\* Where the accumulated balance in RPF becomes taxable, the tax payable in each of the years would be computed as if the fund had been an Unrecognised Provident Fund and the difference in tax would be payable by the employee.

**Note:** If, after termination of his employment with one employer, the employee obtains employment under another employer, then, only so much of the accumulated balance in his provident fund account will be exempt which is transferred to his individual account in a recognised provident fund maintained by the new employer. In such a case, for exemption of payment of accumulated balance by the new employer, the period of service with the former employer shall also be taken into account for computing the period of five years' continuous service.

### ILLUSTRATION 8

Mr. Sohan retires from service on December 31, 2021, after 25 years of service. Following are the particulars of his income/investments for the previous year 2021-22:

Particulars	₹
Basic pay @ ₹ 20,000 per month for 9 months	1,80,000

Dearness pay (50% forms part of the retirement benefits) ₹ 10,000 per month for 9 months	90,000
Lumpsum payment received from the Unrecognised Provident Fund	7,00,000
Deposits in the PPF account	50,000

Out of the amount received from the unrecognized provident fund, the employer's contribution was ₹ 2,80,000 and the interest thereon ₹ 55,000. The employee's contribution was ₹ 3,00,000 and the interest thereon ₹ 65,000. What is the taxable portion of the amount received from the unrecognized provident fund in the hands of Mr. Sohan for the assessment year 2022-23?

### SOLUTION

Taxable portion of the amount received from the URPF in the hands of Mr. Sohan for the A.Y. 2022-23 is computed hereunder:

Particulars	₹
<b>Amount taxable under the head "Salaries":</b>	
Employer's share in the payment received from the URPF	2,80,000
Interest on the employer's share	55,000
<b>Total</b>	<b>3,35,000</b>
<b>Amount taxable under the head "Income from Other Sources":</b>	
Interest on the employee's share	65,000
<b>Total amount taxable from the amount received from the fund</b>	<b>4,00,000</b>

**Note:** The employee is not eligible for deduction under section 80C for his contribution to URPF at the time of such contribution. Hence, the employee's share received from the URPF is not taxable at the time of withdrawal as this amount has already been taxed as his salary income.

### ILLUSTRATION 9

Will your answer be any different if the fund mentioned above was a recognised provident fund?

### SOLUTION

The receipt of accumulated balance in a recognized provident fund would be exempt in the hand of the employee if the employee has rendered continuous service of 5 years or more. In the given case, since the withdrawal is taking place after a service of 25 years, the entire amount received from the RPF will be fully exempt from tax.

### ILLUSTRATION 10

Mr. Bablu is working in ABC Ltd. and has given the details of his income for the P.Y.2021-22. You are required to compute his gross salary from the details given below:

Basic Salary ₹ 12,000 p.m.

<i>D.A. (50% is for retirement benefits)</i>	<i>₹ 9,000 p.m.</i>
<i>Commission as a percentage of turnover</i>	<i>0.1%</i>
<i>Turnover during the year</i>	<i>₹ 60,00,000</i>
<i>Bonus</i>	<i>₹ 50,000</i>
<i>Gratuity</i>	<i>₹ 30,000</i>
<i>His own contribution in the RPF</i>	<i>₹ 25,000</i>
<i>Employer's contribution to RPF</i>	<i>20% of his basic salary</i>
<i>Interest accrued in the RPF@13% p.a.</i>	<i>₹ 13,000</i>

**SOLUTION****Computation of Gross Salary of Mr. Bablu for the A.Y.2022-23**

Particulars	₹	₹
Basic Salary [₹ 12,000 × 12]		1,44,000
Dearness Allowance [₹ 9,000 × 12]		1,08,000
Commission on turnover [0.1% × ₹ 60,00,000]		6,000
Bonus		50,000
Gratuity [Note 1]		30,000
Employers contribution to RPF [20% of ₹1,44,000]	28,800	
Less: Exempt [Note 2]	24,480	4,320
Interest accrued in the RPF@13% p.a.	13,000	
Less: Exempt@9.5% p.a. [₹13,000/13% × 9.5%]	9,500	3,500
<b>Gross Salary</b>		<b>3,45,820</b>

**Note 1:** Gratuity received during service is fully taxable.

**Note 2:** Employers contribution to RPF is exempt up to 12% of salary.

i.e., 12% of [Basic Salary + Dearness Allowance forming part of retirement benefits + Commission based on turnover] = 12% of [₹ 1,44,000 + (50% × ₹ 1,08,000) + ₹ 6,000] = 12% of ₹ 2,04,000 = ₹ 24,480

**Note 3:** Employee's contribution to RPF is not taxable. It is eligible for deduction under section 80C.

**(viii) 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**

National Pension scheme is a scheme approved by the Government for Indian citizen aged between 18-65 years. Subscriber of the NPS account contributes some amount in their account. In case of any employee, being a subscriber of the NPS account, employer may also contribute into the employee's account.

**Employer's contribution to NPS account would form part of salary of employees**

However, while computing total income of the employee-assessee, a deduction under section 80CCD is allowed to the assessee in respect of the employer as well as employee contribution under a pension scheme referred therein. (*Deduction under section 80CCD will be discussed in detail in Chapter 11 – "Deductions from Gross Total Income"*)

**(2) Profits in lieu of salary [Section 17(3)]**

It includes the following:	
<b>(i) Compensation on account of termination of his employment</b>	
	The amount of any compensation due to or received by an assessee from his employer or former employer at or in connection with the termination of his employment.
<b>(ii) Compensation on account of modification of the terms and conditions of employment</b>	
	The amount of any compensation due to or received by an assessee from his employer or former employer at or in connection with the modification of the terms and conditions of employment.
	Usually, such compensation is treated as a capital receipt. However, by virtue of this provision, the same is treated as a revenue receipt and is chargeable as salary.
	<b>Note:</b> It is to be noted that merely because a payment is made by an employer to a person who is his employee does not automatically fall within the scope of the above provisions. The payment must be arising due to master-servant relationship between the payer and the payee. If it is not on that account, but due to considerations totally unconnected with employment, such payment is not profit in lieu of salary.
<b>(iii) Payment from provident fund or other funds</b>	
	Any payment due to or received by an assessee from his employer or former employer from a provident or other fund other than
	- Gratuity [Section 10(10)]
	- Pension [Section 10(10A)]
	- Compensation received by a workman under Industrial Disputes Act, 1947 [Section 10(10B)]
	- from statutory provident fund or public provident fund [Section 10(11)]



- from recognized provident fund [Section 10(12)]
- from approved superannuation fund [Section 10(13)]
- any House Rent Allowance [Section 10(13A)],

to the extent to which it does not consist of employee's contributions or interest on such contributions.

**Note:** If any sum is paid to an employee at the time of maturity from an unrecognised provident fund it is to be dealt with as follows:

- (a) that part of the sum which represents the employer's contribution to the fund and interest thereon is taxable under salaries.
- (b) that part of the sum which represents employee's contribution is not chargeable to tax as no deduction or exemption was available at the time of contribution.
- (c) that part of the sum which represents the interest on employee's contribution is chargeable to tax as 'income from other sources'.

**(iv) Keyman Insurance policy**

Any sum received by an assessee under a Keyman Insurance policy including the sum allocated by way of bonus on such policy.

**(v) Lumpsum Payment or otherwise**

Any amount, whether in lumpsum or otherwise, due to the assessee or received by him, from any person -

- (a) before joining employment with that person, or
- (b) after cessation of his employment with that person.

**(i) Retrenchment compensation**

The retrenchment compensation means the compensation paid under Industrial Disputes Act, 1947 or under any Act, Rule, Order or Notification issued under any law. It also includes compensation paid on transfer of employment under section 25F or closing down of an undertaking under section 25FF of the Industrial Disputes Act, 1947.

It may be noted that compensation on account of termination and due to modification in terms and conditions of employment would be taxable as "profits in lieu of salary". However, the retrenchment compensation would be exempt under section 10(10B), subject to following limits.

- (a) Amount calculated in accordance with the provisions of section 25F of the Industrial Disputes Act, 1947

i.e., 15 days average pay x completed years of service and part thereof in excess of 6 months

**or**

- (b) An amount, not less than ₹ 5,00,000 as may be notified by the Central Government in this behalf, whichever is lower.

**Notes:**

1. *The above limits will not be applicable to cases where the compensation is paid under any scheme approved by the Central Government for giving special protection to workmen under certain circumstances.*
2. *Average pay means average of the wages payable to a workman*
  - *in the case of monthly paid workman, in the three complete calendar months,*
  - *in the case of weekly paid workman, in the four calendar weeks,*
  - *in the case of daily paid workman, in the twelve full working days,*

*preceding the date on which the average pay becomes payable if the workman had worked for three complete calendar months or four complete weeks or twelve full working days, as the case may be, and where such calculation cannot be made, the average pay shall be calculated as the average of the wages payable to a workman during the period he actually worked.*
3. *Wages for this purpose means all remuneration capable of being expressed in terms of money, which would, if the terms of employment, expressed or implied, were fulfilled, be payable to a workman in respect of his employment or of work done in such employment, and includes*
  - *such allowances including DA as the workman is for the time being entitled to;*
  - *the value of any house accommodation, or of supply of light, water, medical attendance or other amenity or of any other service or of any concessional supply of foodgrains or other articles;*
  - *any travel concession; and*
  - *any commission payable on the promotion of sales or business or both*

*However, it does not include*

  - *any bonus;*
  - *contribution to a retirement benefit scheme;*
  - *any gratuity payable on the termination of his service.*

**(ii) Voluntary Retirement Receipts [Section 10(10C)]**

Lumpsum payment or otherwise received by an employee at the time of voluntary retirement would be taxable as “profits in lieu of salary”. However, it would be exempt under section 10(10C), subject to the following conditions:

**Eligible Undertakings** - The employee of the following undertakings are eligible for exemption under this clause:

- (i) Public sector company
- (ii) Any other company
- (iii) An authority established under a Central/State or Provincial Act
- (iv) A local authority
- (v) A co-operative society
- (vi) An University established or incorporated under a Central/ State or Provincial Act and an Institution declared to be an University by the University Grants Commission.
- (vii) An Indian Institute of Technology
- (viii) Such Institute of Management as the Central Government may, by notification in the Official Gazette, specify in this behalf
- (ix) Any State Government
- (x) The Central Government
- (xi) An institution, having importance throughout India or in any State or States, as the Central Government may specify by notification in the Official Gazette.

**Limit:** The maximum limit of exemption should not exceed ₹ 5 lakh.

Such compensation should be at the time of his voluntary retirement or termination of his service, in accordance with any scheme or schemes of voluntary retirement or, in the case of public sector company, a scheme of voluntary separation. The exemption will be available even if such compensation is received in installments.

**Guidelines:**

The schemes should be framed in accordance with such guidelines, as may be prescribed and should include the criteria of economic viability.

**Rule 2BA prescribes the following guidelines for the purposes of the above clause:**

1. It applies to an employee who has completed 10 years of service or completed 40 years of age.  
However, this requirement is not applicable in case of an employee of a public sector company under the scheme of voluntary separation framed by the company.
2. It applies to all employees by whatever name called, including workers and executives of the company or the authority or a co-operative society except directors of a company or a cooperative society.
3. The scheme of voluntary retirement or separation must have been drawn to result in overall reduction in the existing strength of the employees.

4. The vacancy caused by the voluntary retirement or separation must not be filled up.
5. The retiring employee of a company shall not be employed in another company or concern belonging to the same management.
6. The amount receivable on account of voluntary retirement or separation of the employee **must not exceed**
  - the **amount equivalent to three months' salary** for each completed year of service or
  - salary at the time of retirement multiplied by the balance months of service left before the date of his retirement or superannuation.

#### Notes –

1. Where any relief has been allowed to any assessee under section 89 for any assessment year in respect of any amount received or receivable on his voluntary retirement or termination of service or voluntary separation, no exemption under section 10(10C) shall be allowed to him in relation to that assessment year or any other assessment year.
2. Where exemption for voluntary retirement compensation under section 10(10C) has been allowed in any assessment year, then no exemption thereunder shall be allowed to him in any other assessment year.
3. Salary for this purpose means basic salary and dearness allowance, if provided in the terms of employment for retirement benefits, forming part of salary and commission which is expressed as a fixed percentage of turnover.

#### ILLUSTRATION 11

*Mr. Dinesh received voluntary retirement compensation of ₹ 15,00,000 after 30 years 4 months of service in SBI. He still has 6 years of service left. At the time of voluntary retirement, he was drawing basic salary ₹ 30,000 p.m.; Dearness allowance (which forms part of pay) ₹ 10,000 p.m. Compute his taxable voluntary retirement compensation, assuming that he does not claim any relief under section 89.*

#### SOLUTION

Voluntary retirement compensation received	₹ 15,00,000
Less: Exemption under section 10(10C) read with Rule 2BA [See Note below]	<u>₹ 5,00,000</u>
Taxable voluntary retirement compensation	<u>₹ 10,00,000</u>

**Note:** Exemption is to the extent of least of the following:

- (i) Compensation actually received = ₹ 15,00,000

(ii)	Statutory limit	= ₹ 5,00,000
(iii)	Last drawn salary × 3 × completed years of service = (₹ 30,000 + ₹ 10,000) × 3 × 30 years	= ₹ 36,00,000
(iv)	Last drawn salary × remaining months of service = (₹ 30,000 + ₹ 10,000) × 6 × 12 months	= ₹ 28,80,000

### (3) Perquisites

The term 'perquisite' indicates some extra benefit in addition to the amount that may be legally due by way of contract for services rendered. In modern times, the salary package of an employee normally includes monetary salary and perquisites like housing, car etc.

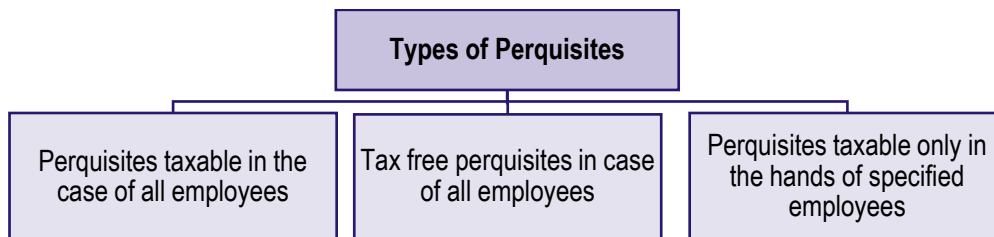
- Perquisite may be provided in cash or in kind.
- Reimbursement of expenses incurred in the official discharge of duties is not a perquisite.
- Perquisite may arise in the course of employment or in the course of profession. If it arises from a relationship of employer-employee, then the value of the perquisite is taxable as salary. However, if it arises during the course of profession, the value of such perquisite is chargeable as profits and gains of business or profession.
- Perquisite will become taxable only if it has a legal origin. An unauthorised advantage taken by an employee without his employer's sanction cannot be considered as a perquisite under the Act.

#### Example 11:

*Mr. A, an employee, is given a house by his employer. On 31.3.2022, he is terminated from service, but he continues to occupy the house without the permission of the employer for six more months after which he is evicted by the employer. The question arises whether the value of the benefit enjoyed by him during the six months period can be considered as a perquisite and be charged to salary. It cannot be done since the relationship of employer-employee ceased to exist after 31.3.2022. However, the definition of income is wide enough to bring the value of the benefit enjoyed by Mr. A to tax as "Income from other sources".*

#### (i) Definition of "Perquisite"

The term "perquisite" is defined under section 17(2). The definition of perquisite is an inclusive one. Based on the definition, perquisites can be classified in following three ways:



**(A) Perquisites taxable in the case of all employees**

The following perquisites are chargeable to tax in case of all employees:

<b>Rent Free Accommodation</b>	Value of rent-free accommodation provided to the assessee by his employer [Section 17(2)(i)]. [Refer discussion on valuation of perquisite]
<i><b>Exception:</b> Rent-free official residence provided to a Judge of a High Court or to a Judge of the Supreme Court is not taxable.</i>	
<b>Concession in rent</b>	Value of concession in rent in respect of accommodation provided to the assessee by his employer [Section 17(2)(ii)].
<b>Payment by the employer in respect of an obligation of employee</b>	Amount paid by an employer in respect of any obligation which otherwise would have been payable by the employee [Section 17(2)(iv)].
<i><b>Example 12:</b> If a domestic servant is engaged by an employee and the employer reimburses the salary paid to the servant, it becomes an obligation which the employee would have discharged even if the employer did not reimburse the same. This perquisite will be covered by section 17(2)(iv) and will be taxable in the hands of all employees.</i>	
<b>Amount payable by an employer directly or indirectly to effect an assurance on the life of the assessee</b>	<p>Amount payable by an employer directly or indirectly to effect an assurance on the life of the assessee or to effect a contract for an annuity, other than payment made to RPF or approved superannuation fund or deposit-linked insurance fund established under the Coal Mines Provident Fund and Miscellaneous Provisions Fund, 1948 or Employees' Provident Fund and Miscellaneous Provisions Act, 1952 [Section 17(2)(v)].</p> <p>However, there are schemes like group annuity scheme, employees state insurance scheme and fidelity insurance scheme, under which insurance premium is paid by employer on behalf of the employees. Such payments are not regarded as perquisite in view of the fact that the employees have only an expectancy of the benefit in such schemes.</p>
<b>Specified security or sweat equity shares allotted or transferred, by the employer</b>	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 [Section 17(2)(vi)] [Refer discussion on valuation of perquisite].
<b>Amount or the aggregate of amounts of any contribution made to the</b>	The amount or aggregate of amounts of any contribution made

<b>account of the assessee by employer</b> <ul style="list-style-type: none"> <li>- in a recognised provident fund</li> <li>- in NPS</li> <li>- in an approved superannuation fund</li> </ul>	<ul style="list-style-type: none"> <li>- in a recognised provident fund</li> <li>- in NPS referred to in section 80CCD(1)</li> <li>- in an approved superannuation fund</li> </ul> by the employer to the account of the assessee, to the extent it exceeds ₹ 7,50,000 [Section 17(2)(vii)].
<b>Annual accretion to the balance at the credit of the recognised provident fund/ NPS/ approved superannuation fund which relates to the employer's contribution and included in total income (on account of the same having exceeded ₹ 7,50,000)</b>	Refer discussion below
<b>Any other fringe benefit or amenity</b>	<p>The value of any other fringe benefit or amenity as may be prescribed by the CBDT [Section 17(2)(viii)].</p> <p>Rule 3(7) prescribed the following other benefits or amenity taxable in case of all the employees.</p> <ul style="list-style-type: none"> <li>- Interest free or concessional loan</li> <li>- Travelling, touring and accommodation</li> <li>- Free or concessional food and non-alcoholic beverages</li> <li>- Gift, voucher or token in lieu of such gift</li> <li>- Credit card expense</li> <li>- Club expenditure</li> <li>- Use of movable assets</li> <li>- Transfer of movable assets</li> <li>- Other benefit or amenity [For valuation, refer discussion on valuation of perquisite]</li> </ul>

**Annual accretion to the balance at the credit of the recognised provident fund/ NPS/ approved superannuation fund which relates to the employer's contribution and included in total income (on account of the same having exceeded ₹ 7,50,000)**

Any annual accretion by way of interest, dividend or any other amount of similar nature during the previous year to the balance at the credit of the recognized provident fund or NPS or approved superannuation fund to the extent it relates to the employer's contribution which is included in total income in any previous year under section 17(2)(vii) computed in prescribed manner [Section 17(2)(viii)].

In other words, interest, dividend or any other amount of similar nature on the amount which is included in total income under section 17(2)(vii) would also be treated as a perquisite.

The CBDT has, vide Rule 3B, notified the following manner to compute the annual accretion by way of interest, dividend or any other amount of similar nature during the previous year-

$$TP = (PC/2)*R + (PC1 + TP1)*R$$

Where,

TP	Taxable perquisite under section 17(2)(vii) for the current previous year
PC	Amount or aggregate of amounts of employer's contribution in excess of ₹ 7.5 lakh to recognized provident fund, national pension scheme u/s 80CCD and approved superannuation fund during the previous year
PC1	Amount or aggregate of amounts of employer's contribution in excess of ₹ 7.5 lakh to recognized provident fund, national pension scheme u/s 80CCD and approved superannuation fund for the previous year or years commencing on or after 1 <sup>st</sup> April, 2020 other than the current previous year
TP1	Aggregate of taxable perquisite under section 17(2)(vii) for the previous year or years commencing on or after 1 <sup>st</sup> April, 2020 other than the current previous year
R	I/ Favg
I	Amount or aggregate of amounts of income accrued during the current previous year in recognized provident fund, national pension scheme u/s 80CCD and approved superannuation fund
Favg	(Amount or aggregate of amounts of balance to the credit of recognized provident fund, national pension scheme u/s 80CCD and approved superannuation fund on 1 <sup>st</sup> April, 2021 + Amount or aggregate of amounts of balance to the credit of recognized provident fund, national pension scheme u/s 80CCD and approved superannuation fund on 31 <sup>st</sup> March, 2022)/2

Where the amount or aggregate of amounts of TP1 and PC1 exceeds the amount or aggregate of amounts of balance to the credit of the specified fund or scheme on 1<sup>st</sup> April, 2021, then, the amount in excess of the amount or aggregate of amounts of the said balance shall be ignored for the purpose of computing the amount or aggregate of amounts of TP1 and PC1.

#### ILLUSTRATION 12

Mr. X is appointed as a CFO of ABC Ltd. in Mumbai from 1.5.2020. His basic salary is ₹ 5,50,000 p.m. He is paid 10% as D.A. He contributes 11% of his pay and D.A. towards his recognized provident fund and the company contributes the same amount. The accumulated balance in recognized provident fund as on 1.4.2021 and 31.3.2022 is ₹ 15,35,000 and ₹ 33,55,000, respectively. Compute the perquisite value chargeable in the hands of Mr. X u/s 17(2)(vii) and 17(2)(vii) for the P.Y. 2021-22.



**SOLUTION**

1. Perquisite value taxable u/s 17(2)(vii) = ₹ 7,98,600, being employer's contribution to recognized provident fund during the P.Y. 2021-22 – ₹ 7,50,000 = ₹ 48,600
2. Annual accretion on perquisite taxable u/s 17(2)(vii) =  $(PC/2)*R + (PC1 + TP1)*R$   
 $= (48,600/2)*0.091 + 0$   
 $= ₹ 2,211$ 

PC     ABC Ltd.'s contribution in excess of ₹ 7.5 lakh to recognized provident fund during P.Y. 2021-22 = ₹ 48,600

PC1    Nil since employer's contribution is less than ₹ 7.5 lakh to recognized provident fund in P.Y. 2020-21.

TP1    Nil

R      $I/F_{avg} = 2,22,800/24,45,000 = 0.091$

I     RPF balance as on 31.3.2022 – employee's and employer's contribution during the year – RPF balance as on 1.4.2021 = ₹ 2,22,800 (₹ 33,55,000 – ₹ 7,98,600 – ₹ 7,98,600 – ₹ 15,35,000)

Favg   Balance to the credit of recognized provident fund as on 1<sup>st</sup> April, 2021 + Balance to the credit of recognized provident fund as on 31<sup>st</sup> March, 2022)/2 = (₹ 15,35,000 + ₹ 33,55,000)/2 = ₹ 24,45,000

**Note** – Since the employee's contribution to RPF exceeds ₹ 2,50,000 in the P.Y. 2021-22, interest on ₹ 5,48,600 (i.e., ₹ 7,98,600 – ₹ 2,50,000) will also be chargeable to tax.

**Exemption in respect of Payment from superannuation funds [Section 10(13)]**

Any payment received by any employee from an approved superannuation fund shall be entirely excluded from his total income if the payment is made

- (a) to the legal heirs on the death of beneficiary (e.g. payment to widow of the beneficiary); or
- (b) to an employee in lieu of or in commutation of an annuity on his retirement at or after the specified age or on his becoming incapacitated prior to such retirement; or
- (c) by way of refund of contribution on the death of the beneficiary; or,
- (d) by way of refund of contribution to an employee on his leaving the service in connection with which the fund is established otherwise than by retirement at or after a specified age or his becoming incapacitated prior to such retirement, to the extent the payment made does not exceed the contribution made prior to 1-4-1962 and the interest thereon.

For example, where the amount received by an employee does not include any contribution made prior to 1.4.1962, the whole amount is taxable.

- (e) by way of transfer to the account of the employee under a pension scheme referred to in section 80CCD, which is notified by the Central Government.

**(B) Tax free perquisites in all cases**

The following perquisites are exempt from tax in the hands of all employees.

<b>Telephone</b>	Telephone provided by an employer to an employee at his residence
<b>Transport Facility</b>	Transport facility provided by an employer engaged in the business of carrying of passengers or goods to his employees either free of charge or at concessional rate;
<b>Privilege passes and privilege ticket</b>	Privilege passes and privilege ticket orders granted by Indian Railways to its employees;
<b>Perquisites allowed outside India by the Government</b>	Perquisites allowed outside India by the Government to a citizen of India for rendering services outside India;
<b>Employer's contribution to staff group insurance scheme;</b>	Employer's contribution to staff group insurance scheme;
<b>Annual premium by employer on personal accident policy</b>	Payment of annual premium by employer on personal accident policy effected by him on the life of the employee;
<b>Refreshment</b>	Refreshment provided to all employees during working hours in office premises;
<b>Subsidized lunch</b>	Subsidized lunch provided to an employee during working hours at office or business premises provided the value of such meal is upto ₹ 50;
<b>Recreational facilities</b>	Recreational facilities, including club facilities, extended to employees in general i.e., not restricted to a few select employees;
<b>Amount spent on training of employees</b>	Amount spent by the employer on training of employees or amount paid for refresher management course including expenses on boarding and lodging;
<b>Sum payable by employer to a RPF or an approved superannuation fund</b>	Sum payable by an employer to a RPF or an approved superannuation fund or deposit-linked insurance fund established under the Coal Mines Provident Fund and Miscellaneous provisions Act, 1948 or the Employees' Provident Fund and Miscellaneous Provisions Act, 1952 upto the limit prescribed;
<b>Leave travel concession</b>	Leave travel concession, subject to the conditions specified under section 10 (discussed below)
<b>Note:</b> Value of Leave travel concession provided to the High Court judge or the Supreme Court Judge and members of his family are completely exempt without any conditions.	

<b>Medical facilities</b>	Medical facilities subject to certain prescribed limits;
<b>Rent-free official residence</b>	Rent-free official residence provided to a Judge of a High Court or the Supreme Court;
<b>Conveyance facility</b>	Conveyance facility provided to High Court Judges under section 22B of the High Court Judges (Conditions of Service) Act, 1954 and Supreme Court Judges under section 23A of the Supreme Court Judges (Conditions of Service) Act, 1958.

***Exemption in respect of Leave travel concession [Section 10(5)]***

- (i) This clause exempts the leave travel concession (LTC) received by employees from their employers for proceeding to any place in India,
  - (a) either on leave or
  - (b) after retirement from service or
  - (c) after termination of his service.
- (ii) **The benefit is available to individuals** - citizens as well as non-citizens - in respect of travel concession or assistance for himself or herself and for his/her family- *i.e.*, spouse and children of the individual and parents, brothers and sisters of the individual or any of them wholly or mainly dependent on the individual.
- (iii) **Limit of exemption** - The exemption in all cases will be limited to the amount actually spent subject to such conditions as specified in Rule 2B regarding the ceiling on the number of journeys for the place of destination.

Under Rule 2B, exemption will be available in respect of 2 journeys performed in a block of 4 calendar years commencing from the calendar year 1986. Where such travel concession or assistance is not availed by the individual during any block of 4 calendar years, one such unavailed LTC will be carried forward to the immediately succeeding block of 4 calendar years and will be eligible for exemption.

***Example 13:***

*An employee does not avail any LTC for the block 2018-21. He is allowed to carry forward maximum one unavailed LTC to be used in the succeeding block of 2022-25. Accordingly, if he avails LTC in April, 2022, the same will be treated as having availed in respect of the block 2018-2021. Therefore, he will be eligible for exemption in respect of that journey and two more journeys can be further availed in respect of the block of 2022-25.*

- (iv) **Monetary limits** - Where the journey is performed on or after the 1.10.1997, the amount exempted under section 10(5) in respect of the value of LTC shall be the amount actually incurred on such travel subject to the following conditions:

S.No.	Journey performed by	Limit
1	Air	Amount not exceeding the air economy fare of the National Carrier by the shortest route to the place of destination
2	Any other mode: (i) Where rail service is available (ii) Where rail service is not available (a) a recognised public transport system exists (b) no recognised public transport system exists	Amount not exceeding the air-conditioned first class rail fare by the shortest route to the place of destination  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  amount equivalent to the air-conditioned first class rail fare, for the distance of the journey by the shortest route, as if the journey had been performed by rail

**Note:** The exemption referred to shall not be available to more than two surviving children of an individual after 1.10.1998. This restrictive sub-rule shall not apply in respect of children born before 1.10.1998 and also in case of multiple births after one child.

#### ILLUSTRATION 13

*Mr. Dinesh went on a holiday on 10.12.2021 to Kerala with his wife and three children (one daughter – age 4 years; twin sons – age 2 years). They went by flight (economy class) and the total cost of tickets reimbursed by his employer was ₹ 50,000 (₹ 35,000 for adults and ₹ 15,000 for the three minor children). Compute the amount of LTC exempt assuming that he has previously availed the exemption only once, in the block of four calendar years.*

#### SOLUTION

Since the daughter's age is more than the twin sons, Mr. Dinesh can avail exemption for all his three children. The restriction of two children is not applicable to multiple births after one child. The holiday being in India and the journey being performed by air (economy class), the entire reimbursement met by the employer is fully exempt under section 10(5) read with rule 2B.

#### ILLUSTRATION 14

*In the above illustration 13, will there be any difference if among his three children the twins were 4 years old and the daughter 2 years old? Examine.*

**SOLUTION**

Since the twins' age is more than the daughter, Mr. Dinesh cannot avail for exemption for all his three children. The LTC exemption can be availed in respect of only two children. Therefore,

$$\text{taxable LTC} = 15,000 \times \frac{1}{3} = ₹ 5,000 .$$

LTC exempt is only ₹ 55,000 (i.e. ₹ 60,000 – ₹ 5,000)

**Medical facilities (Proviso to section 17(2))**

The following medical facilities **will not** amount to a perquisite:

- (i) **Value of medical treatment in any hospital maintained by the employer:** The value of any medical treatment provided to an employee or any member of his family in any hospital maintained by the employer;
- (ii) **Reimbursement of expenditure actually incurred on medical treatment:** Any sum paid by the employer in respect of any expenditure actually incurred by the employee on his medical treatment or treatment of any member of his family
  - **in any hospital** maintained by the Government/local authority/any other hospital approved by the Government for the purpose of medical treatment of its employees;
  - **in respect of the prescribed disease** or ailments in any hospital approved by the Principal Chief Commissioner or Chief Commissioner having regard to the prescribed guidelines.

However, in order to claim this benefit, the employee shall attach 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.

Thus, the two types of facilities are covered:

- (a) payment by the employer for treatment in a Government hospital and
  - (b) payment by an employer for treatment of prescribed diseases in any hospital approved by the principal Chief Commissioner or Chief Commissioner.
- (iii) **Premium paid to effect an insurance on the health of employee:** Any premium paid by an employer in relation to an employee to effect an insurance on the health of such employee. However, any such scheme should be approved by the Central Government or the Insurance Regulatory Development Authority (IRDA) for the purposes of section 36(1)(ib).
  - (iv) **Reimbursement of premium paid to effect an insurance on the health of employee or for the family of an employee:** Any sum paid by the employer in respect of any premium paid by the employee to effect an insurance on his health or the health of any member of

his family under any scheme approved by the Central Government or the Insurance Regulatory Development Authority (IRDA) for the purposes of section 80D.

- (v) **Amount paid towards expenditure incurred outside India on medical treatment:** Any expenditure incurred by the employer or any sum paid by the employer on any expenditure actually incurred by the employee on the following:
- (a) **medical treatment** of the employee or any member of the family of such employee outside India;
  - (b) **travel and stay abroad** of the employee or any member of the family of such employee for medical treatment;
  - (c) **travel and stay abroad of one attendant** who accompanies the patient in connection with such treatment.

**Conditions:**

1. The perquisite element in respect of expenditure on medical treatment and stay abroad will be exempt only to the extent permitted by the RBI.
2. The expenses in respect of traveling of the patient and the attendant will be exempt if the employee's gross total income as computed before including the said expenditure does not exceed ₹ 2 lakh.

**Note:** For this purpose, family means spouse and children of the individual. Children may be dependent or independent, married or unmarried. It also includes parents, brothers and sisters of the individual if they are wholly or mainly dependent upon him. Hospital includes a dispensary or a clinic or a nursing home.

**ILLUSTRATION 15**

*Compute the taxable value of the perquisite in respect of medical facilities received by Mr. Ganesh from his employer during the P.Y.2021-22:*

<i>Medical premium paid for insuring health of Mr. Ganesh</i>	<i>₹ 14,000</i>
<i>Treatment of Mr. Ganesh by his family doctor</i>	<i>₹ 10,000</i>
<i>Treatment of Mrs. Ganesh in a Government hospital</i>	<i>₹ 30,000</i>
<i>Treatment of Mr. Ganesh's grandfather in a private clinic</i>	<i>₹ 12,000</i>
<i>Treatment of Mr. Ganesh's mother (68 years and dependant) by family doctor</i>	<i>₹ 10,000</i>
<i>Treatment of Mr. Ganesh's sister (dependant) in a nursing home</i>	<i>₹ 5,000</i>
<i>Treatment of Mr. Ganesh's brother (independent)</i>	<i>₹ 8,000</i>
<i>Treatment of Mr. Ganesh's father (75 years and dependant) abroad</i>	<i>₹ 60,000</i>

Expenses of staying abroad of the patient and ₹ 40,000

Limit specified by RBI ₹ 75,000

### SOLUTION

#### Computation of taxable value of perquisite in the hands of Mr. Ganesh

Particulars	₹	₹
Treatment of Mrs. Ganesh, being a family member, in a Government hospital		-
Treatment of Mr. Ganesh's father (75 years and dependant) abroad	60,000	
Expenses of staying abroad of the patient and attendant	40,000	
	1,00,000	
Less: Exempt up to limit specified by RBI	75,000	25,000
Medical premium paid for insuring health of Mr. Ganesh		-
Treatment of Mr. Ganesh by his family doctor		10,000
Treatment of Mr. Ganesh's mother (dependant) by family doctor		10,000
Treatment of Mr. Ganesh's sister (dependant) in a nursing home		5,000
Treatment of Mr. Ganesh's grandfather in a private clinic		12,000
Treatment of Mr. Ganesh's brother (independent)		8,000
<b>Taxable value of perquisite</b>		<b>70,000</b>

**Note:** Grandfather and independent brother are not included within the meaning of family of Mr. Ganesh.

#### **Payment of premium on personal accident insurance policies**

If an employer takes personal accident insurance policies on the life of employees and pays the insurance premium, no immediate benefit would become payable and benefit will accrue at a future date only if certain events take place.

Moreover, the employers would be taking such policy in their business interest only, so as to indemnify themselves from payment of any compensation. Therefore, the premium so paid will not constitute a taxable perquisite in the employees' hands [*CIT vs. Lala Shri Dhar [1972] 84 ITR 192 (Del.)*].

#### **(C) Perquisites taxable only in the hands of specified employees [Section 17(2)(iii)]**

Any monetary obligation of the employee which is discharged by the employer is perquisite in the hands of all employees as per section 17(2)(iv). However, sometimes instead of discharging employee's obligation, employer provides perquisites in the form of facility to the employee. Such perquisites are taxable in the hands of specified employees only.

The value of any benefit or amenity granted or provided free of cost or at concessional rate which have not been included in (A) & (B) above will be taxable in the hands of specified employees. Followings are the example of such services:

- (i) Provision of sweeper, gardener, watchman or personal attendant
- (ii) Facility of use of gas, electricity or water supplied by employer
- (iii) Free or concessional tickets
- (iv) Use of motor car
- (v) Free or concessional educational facilities

*For valuation of such perquisites, refer discussion on valuation of perquisite*

### Meaning of Specified employees:

- (i) **Director employee:** An employee of a company who is also a director is a specified employee. It is immaterial whether he is a full-time director or part-time director. It also does not matter whether he is a nominee of the management, workers, financial institutions or the Government. It is also not material whether or not he is a director throughout the previous year.
- (ii) **An employee who has substantial interest in the company:** An employee of a company who has substantial interest in that company is a specified employee. A person has a substantial interest in a company if he is a beneficial owner of equity shares carrying 20% or more of the voting power in the company.

**Beneficial and legal ownership:** In order to determine whether a person has a substantial interest in a company, it is the beneficial ownership of equity shares carrying 20% or more of the voting power that is relevant rather than the legal ownership.

#### **Example 14:**

*A, Karta of a HUF, is a registered shareholder of Bright Ltd. The amount for purchasing the shares is financed by the HUF. The dividend is also received by the HUF. Supposing further that A is an employee in Bright Ltd., the question arises whether he is a specified employee.*

*In this case, he cannot be called a specified person since he has no beneficial interest in the shares registered in his name. It is only for the purpose of satisfying the statutory requirements that the shares are registered in the name of A. All the benefits arising from the shareholding goes to the HUF. Conversely, it may be noted that an employee who is not a registered shareholder will be considered as a specified employee if he has beneficial interest in 20% or more of the equity shares in the company.*

- (iii) **Employee drawing in excess of ₹ 50,000:** An employee other than an employee described in (i) & (ii) above, whose income chargeable under the head 'salaries' exceeds ₹ 50,000 is a specified employee. The above salary is to be considered exclusive of the value of all benefits or amenities not provided by way of monetary payments.



**In other words, for computing the limit of ₹ 50,000, the following items have to be excluded or deducted:**

(a)	all non-monetary benefits;
(b)	monetary benefits which are exempt under section 10. This is because the exemptions provided under section 10 are excluded completely from salaries. For example, HRA or education allowance or hostel allowance are not to be included in salary to the extent to which they are exempt under section 10.
(c)	Standard deduction upto <b>₹ 50,000</b> [under section 16(ia)], Deduction for entertainment allowance [under section 16(ii)] and deduction toward professional tax [under section 16(iii)] are also to be excluded.

If an employee is employed with more than one employer, the aggregate of the salary received from all employers is to be taken into account in determining the above ceiling limit of ₹ 50,000, i.e., Salary for this purpose = Basic Salary + Dearness Allowance + Commission, whether payable monthly or turnover based + Bonus + Fees + Any other taxable payment + Any taxable allowances + Any other monetary benefits – Deductions under section 16]

## (ii) Valuation of Perquisites

The Income-tax Rules, 1962 contain the provisions for valuation of perquisites. It is important to note that only those perquisites which the employee actually enjoys have to be valued and taxed in his hand.

### Example 15:

*Suppose a company offers a housing accommodation rent-free to an employee but the latter declines to accept it, then the value of such accommodation obviously cannot be evaluated and taxed in the hands of the employees.*

For the purpose of computing the income chargeable under the head “Salaries”, the value of perquisites provided by the employer directly or indirectly to the employee or to any member of his household by reason of his employment shall be determined in accordance with **Rule 3**.

### (A) Valuation of residential accommodation [Sub-rule (1) of Rule 3]

The value of residential accommodation provided by the employer during the previous year shall be determined in the following manner –

Sl. No.	Circumstances	In case of unfurnished accommodation	In case of furnished accommodation
(1)	(2)	(3)	(4)
1.	Where the accommodation is provided by the Central	<ul style="list-style-type: none"> <li>License fee determined by the Central Government or any State Government in</li> </ul>	<ul style="list-style-type: none"> <li>The value of perquisite as determined under column (3) should be</li> </ul>

	<p><b>Government or any State Government to the employees either holding office or post in connection with the affairs of the Union or of such State</b></p>	<p>respect of accommodation in accordance with the rules framed by such Government</p> <p><b>as reduced by</b></p> <ul style="list-style-type: none"> <li>the rent actually paid by the employee.</li> </ul>	<p><b>increased by</b></p> <p>(i) <b>If furniture is owned by employer,</b></p> <p>10% per annum of the cost of furniture (including television sets, radio sets, refrigerators, other household appliances, air-conditioning plant or equipment).</p> <p>(ii) <b>If such furniture is hired from a third party,</b></p> <ul style="list-style-type: none"> <li>The actual hire charges payable for the same</li> </ul> <p><b>as reduced by</b></p> <ul style="list-style-type: none"> <li>any charges paid or payable for the same by the employee during the previous year</li> </ul>
2.	<p><b>Where the accommodation is provided by any other employer</b></p> <p>(a) <u>where the accommodation is owned by the employer</u></p>	<p>(i) 15% of salary in cities having population &gt; 25 lakhs as per 2001 census;</p> <p>(ii) 10% of salary in cities having population &gt; 10 lakhs ≤ 25 lakhs as per 2001 census;</p> <p>(iii) 7.5% of salary in other areas,</p> <p>in respect of the period during which the said accommodation was occupied by the employee during the previous year</p> <p><b>as reduced by</b></p>	<ul style="list-style-type: none"> <li>The value of perquisite as determined under column (3) should be</li> </ul> <p><b>increased by</b></p> <p>(i) <b>If furniture is owned by employer,</b></p> <p>10% per annum of the cost of furniture (including television sets, refrigerators, other household appliances, air-conditioning plant or equipment or other similar appliances or gadgets).</p> <p>(ii) <b>If such furniture is hired from a third party,</b></p> <ul style="list-style-type: none"> <li>the actual hire charges payable for the same</li> </ul> <p><b>as reduced by</b></p>

		the rent, if any, actually paid by the employee.	<ul style="list-style-type: none"> <li>any charges paid or payable for the same by the employee during the previous year</li> </ul>
	(b) <u>where the accommodation is taken on lease or rent by the employer</u>	<ul style="list-style-type: none"> <li>Actual amount of lease rental paid or payable by the employer or</li> <li>15% of salary</li> </ul> <p>whichever is lower,</p> <p><b>as reduced by</b></p> <ul style="list-style-type: none"> <li>the rent, if any, actually paid by the employee.</li> </ul>	<ul style="list-style-type: none"> <li>The value of perquisite as determined under column (3) should be</li> </ul> <p><b>increased by</b></p> <p>(i) <b>If furniture is owned by employer,</b></p> <p>10% per annum of the cost of furniture (including television sets, radio sets, refrigerators, other household appliances, air-conditioning plant or equipment or other similar appliances or gadgets).</p> <p>(ii) <b>If such furniture is hired from a third party,</b></p> <ul style="list-style-type: none"> <li>the actual hire charges payable for the same</li> </ul> <p><b>as reduced by</b></p> <ul style="list-style-type: none"> <li>any charges paid or payable for the same by the employee during the previous year</li> </ul>
3.	<b>Where the accommodation is provided by any employer, whether Government or any other employer, in a hotel.</b>	Not applicable	<ul style="list-style-type: none"> <li>24% of salary paid or payable for the previous year or</li> <li>the actual charges paid or payable to such hotel,</li> </ul> <p><b>whichever is lower,</b> for the period during which such accommodation is provided</p> <p><b>as reduced by</b></p> <ul style="list-style-type: none"> <li>the rent, if any, actually paid or payable by the employee.</li> </ul> <p>However, where the employee is provided such accommodation for a period not exceeding in aggregate fifteen days on his transfer from one place to another, there would be no perquisite.</p>

**Notes:**

- (1) If an employee is provided with accommodation, on account of his transfer from one place to another, at the new place of posting while retaining the accommodation at the other place, the value of perquisite shall be determined with reference to only one such accommodation which has the lower perquisite value, as calculated above, for a period not exceeding 90 days and thereafter, the value of perquisite shall be charged for both such accommodations.
- (2) Any accommodation provided to an employee working at a mining site or an on-shore oil exploration site or a project execution site, or a dam site or a power generation site or an off-shore site would not be treated as a perquisite, provided it satisfies either of the following conditions -
  - (i) the accommodation is of temporary nature, has plinth area not exceeding 800 square feet and is located not less than eight kilometers away from the local limits of any municipality or a cantonment board; or
  - (ii) the accommodation is located in a remote area i.e., an area that is located at least 40 kms away from a town having a population not exceeding 20,000 based on latest published all-India census.
- (3) Where the accommodation is provided by the Central Government or any State Government to an employee who is serving on deputation with any body or undertaking under the control of such Government,-
  - (i) the employer of such an employee shall be deemed to be that body or undertaking where the employee is serving on deputation; and
  - (ii) the value of perquisite of such an accommodation shall be the amount calculated in accordance with Sl. No.2.(a) of the above table, as if the accommodation is owned by the employer.
- (4) "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.
- (5) "Hotel" includes licensed accommodation in the nature of motel, service apartment or guest house.
- (B) **Value of any concession in the matter of rent respecting any accommodation provided to the assessee by the employer [Section 17(2)(ii)]**
  - (i) **In case of unfurnished accommodation provided to employees other than Government employees –**
    - **If accommodation owned by the employer:** The difference between the specified rate in respect of the period during which said accommodation was occupied by the assessee and the amount of rent recoverable/recovered from the employee would be deemed to be the concession in the matter of rent.

- **If accommodation taken on lease or rent by the employer:** The difference between the actual lease rent or 15% of salary, whichever is lower, in respect of the period during which said accommodation was occupied by the assessee and rent recovered/recoverable from the employee would be deemed to be the concession in the matter of rent.

(1)	(2)
Type of accommodation	Deemed concession in the matter of rent
<b>Accommodation owned by the employer</b>	<b>Specified rate minus rent recoverable from the employee</b>
In cities having a population > 25 lakh	15% of salary minus rent recoverable from the employee.
In cities having a population > 10 lakh ≤ 25 lakh	10% of salary minus rent recoverable from the employee.
In other cities	7½% of salary minus rent recoverable from employee.
<b>Accommodation taken on lease by the employer</b>	Rent paid by the employer or 15% of salary, whichever is lower, minus rent recoverable from the employee.

- (ii) **In case of furnished accommodation provided to employees other than Government employees**

The difference between hire charges paid or 10% p.a. of cost of furniture, as the case may be, in respect of the period during which said accommodation was occupied by the assessee and the charges paid or payable by the employee would be added to the value determined in column (2) above for determining whether there is a concession in the matter of rent.

- (iii) **In case of furnished accommodation provided to Government employees**

The excess of licence fees determined by the employer as increased by hire charges paid or 10% p.a. of cost of furniture, as the case may be, in respect of the period during which said accommodation was occupied by the assessee over and above the rent recovered/recoverable from the employee and the charges paid or payable for furniture by the employee would be deemed to be the concession in the matter of rent.

- (iv) **In case the accommodation is provided by any employer, whether Government or any other employer, in a hotel**

The difference between the actual charges paid to hotel or 24% of salary, whichever is lower, for the period during which such accommodation is provided and rent recovered/recoverable from the employee would be deemed to be the concession in the matter of rent.

However, where the employee is provided such accommodation for a period not exceeding in aggregate fifteen days on his transfer from one place to another, there would be no perquisite

**Note – Once there is a deemed concession, the provisions of Rule 3(1) discussed above would be applicable in computing the taxable perquisite.**

### **Meaning of Salary**

“Salary” includes pay, allowances, bonus or commission payable monthly or otherwise or any monetary payment, by whatever name called, from one or more employers, as the case may be. However, it does not include the following, namely–

- (1) dearness allowance or dearness pay unless it enters into the computation of superannuation or retirement benefits of the employee concerned;
- (2) employer’s contribution to the provident fund account of the employee;
- (3) allowances which are exempted from the payment of tax;
- (4) value of the perquisites specified in section 17(2);
- (5) any payment or expenditure specifically excluded under the proviso to section 17(2) i.e., payment of medical insurance premium specified therein.

### **ILLUSTRATION 16**

*Mr. Himesh is a Manager in XYZ Ltd. The company has provided him with rent-free unfurnished accommodation in Mumbai. He gives you the following particulars:*

<i>Basic salary</i>	<i>₹ 30,000 p.m.</i>
<i>Dearness Allowance</i>	<i>₹ 7,000 p.m. (30% is for retirement benefits)</i>
<i>Bonus</i>	<i>₹ 3,000 p.m.</i>

*Even though the company allotted the house to him on 1.4.2021, he occupied the same only from 1.11.2021. Calculate the taxable value of the perquisite for A.Y.2022-23.*

### **SOLUTION**

Value of the rent free unfurnished accommodation in respect of the period during which the accommodation is occupied by Mr. Himesh

= 15% of salary for the relevant period

= 15% of [(₹ 30,000 × 5) + (₹ 7,000 × 30% × 5) + (₹ 3,000 × 5)] **[See Note below]**

= 15% of ₹ 1,75,500 = ₹ 26,325.

**Note:** The accommodation is provided in a city having population exceeding 25 Lakhs. Since, Mr. Himesh occupies the house only from 1.11.2021, we have to include the salary due to him only in respect of months during which he has occupied the accommodation. Hence salary for 5 months (i.e. from 1.11.2021 to 31.03.2022) will be considered.

**ILLUSTRATION 17**

*Using the data given in the previous illustration 16, compute the value of the perquisite if Mr. Himesh is required to pay a rent of ₹ 1,000 p.m. to the company, for the use of this accommodation.*

**SOLUTION**

First of all, we have to see whether there is a concession in the matter of rent. In the case of accommodation owned by the employer in cities having a population exceeding ₹ 25 lakh, there would be deemed to be a concession in the matter of rent if 15% of salary exceeds rent recoverable from the employee.

In this case, 15% of salary would be ₹ 26,325 (i.e. 15% of ₹ 1,75,500). The rent paid by the employee is ₹ 5,000 (i.e., ₹ 1,000 × 5). Since 15% of salary exceeds the rent recovered from the employee, there is a deemed concession in the matter of rent. Once there is a deemed concession, the provisions of Rule 3(1) would be applicable in computing the taxable perquisite.

Value of the rent free unfurnished accommodation = ₹ 26,325

Less: Rent paid by the employee (₹ 1,000 × 5) = ₹ 5,000

**Perquisite value of unfurnished accommodation given at concessional rent = ₹ 21,325**

**ILLUSTRATION 18**

*Using the data given in illustration 16, compute the value of the perquisite if XYZ Ltd. has taken this accommodation on a lease rent of ₹ 5,000 p.m. and Mr. Himesh is required to pay a rent of ₹ 1,000 p.m. to the company, for the use of this accommodation.*

**SOLUTION**

Here again, we have to see whether there is a concession in the matter of rent. In the case of accommodation taken on lease by the employer, there would be deemed to be a concession in the matter of rent if the rent paid by the employer or 15% of salary, whichever is lower, exceeds rent recoverable from the employee.

In this case, 15% of salary is ₹ 26,325 (i.e. 15% of ₹ 1,75,500). Rent paid by the employer is ₹ 25,000 (i.e. ₹ 5,000 × 5). The lower of the two is ₹ 25,000, which exceeds the rent paid by the employee i.e. ₹ 5,000 (₹ 1,000 × 5). Therefore, there is a deemed concession in the matter of rent. Once there is a deemed concession, the provisions of Rule 3(1) would be applicable in computing the taxable perquisite.

Value of the rent free unfurnished accommodation [Note] = ₹ 25,000

Less: Rent paid by the employee (₹ 1,000 × 5) = ₹ 5,000

**Value of unfurnished accommodation given at concessional rent = ₹ 20,000**

**Note:** Value of the rent free unfurnished accommodation is lower of

- (i) Lease rent paid by the company for relevant period = ₹ 5,000 × 5 = ₹ 25,000
- (ii) 15% of salary for the relevant period (computed earlier) = ₹ 26,325

#### ILLUSTRATION 19

*Using the data given in illustration 16, compute the value of the perquisite if XYZ Ltd. has provided a Sofa set (WDV ₹ 10,000; Cost ₹ 25,000) and two air conditioners. The rent paid by the company for the air conditioners is ₹ 500 p.m. each. The Sofa set was provided on 1.1.2022. However, Mr. Himesh is required to pay a rent of ₹ 1,000 p.m. to the company, for the use of this furnished accommodation.*

#### SOLUTION

Here again, we have to see whether there is a concession in the matter of rent. In the case of accommodation owned by the employer in a city having a population exceeding ₹ 25 lakh, there would be deemed to be a concession in the matter of rent if 15% of salary exceeds rent recoverable from the employee. In case of furnished accommodation, the excess of hire charges paid or 10% p.a. of the cost of furniture, as the case may be, over and above the charges paid or payable by the employee has to be added to the value arrived at above to determine whether there is a concession in the matter of rent.

In this case, 15% of salary is ₹ 26,325 (i.e. 15% of ₹ 1,75,500). The rent paid by the employee is ₹ 5,000 (i.e. ₹ 1,000 × 5). The value of furniture of ₹ 5,625 (**see Note below**) is to be added to 15% of salary. The deemed concession in the matter of rent is ₹ 26,325 + ₹ 5,625 - ₹ 5,000 = ₹ 26,950. Once there is a deemed concession, the provisions of Rule 3(1) would be applicable in computing the taxable perquisite.

Value of the rent free unfurnished accommodation (computed earlier)	= ₹ 26,325
Add: Value of furniture provided by the employer [ <b>Note</b> ]	= <u>₹ 5,625</u>
Value of rent free furnished accommodation	= ₹ 31,950
Less: Rent paid by the employee (₹ 1,000 × 5)	= <u>₹ 5,000</u>
<b>Value of furnished accommodation given at concessional rent</b>	<b>= <u>₹ 26,950</u></b>

**Note:** Value of the furniture provided = (₹ 500 p.m. × 2 × 5 months) + (₹ 25,000 × 10% p.a. for 3 months) = ₹ 5,000 + ₹ 625 = ₹ 5,625

#### ILLUSTRATION 20

*Using the data given in illustration 19 above, compute the value of the perquisite if Mr. Himesh is a government employee. The licence fees determined by the Government for this accommodation was ₹ 800 p.m.*



**SOLUTION**

In the case of Government employees, the excess of licence fees determined by the employer as increased by the value of furniture and fixture over and above the rent recovered/ recoverable from the employee and the charges paid or payable for furniture by the employee would be deemed to be the concession in the matter of rent. Therefore, the deemed concession in the matter of rent is ₹ 4,625 [i.e. ₹ 4,000 (licence fees: ₹ 800 × 5) + ₹ 5,625 (Value of furniture) – ₹ 5,000 (₹ 1,000 × 5)]. Once there is a deemed concession, the provisions of Rule 3(1) would be applicable in computing the taxable perquisite.

Value of the rent free unfurnished accommodation (₹ 800 × 5) = ₹ 4,000

Add: Value of furniture provided by the employer (computed earlier) = ₹ 5,625

**Value of rent free furnished accommodation = ₹ 9,625**

Less: Rent paid by the employee (₹ 1,000 × 5) = ₹ 5,000

**Perquisite value of furnished accommodation given at concessional rent = ₹ 4,625**

**(C) Motor Car [Sub-rule (2) of Rule 3]**

If motor car is provided by the employer to the employee, it will be perquisite in the hands of specified employees only. However, the use of any vehicle provided by a company or an employer for journey by the assessee from his residence to his office or other place of work, or from such office or place to his residence shall not be regarded as a benefit given or provided to him free of cost or at concessional rate [*Explanation* below section 17(2)(iii)].

But if the motor car is owned by the employee and used by him or members of his family wholly for personal purpose and for which employer reimburses the running and maintenance expenses of the car, it will be perquisite in the hands of all employees.

The value of perquisite by way of use of motor car to an employee by an employer shall be determined in the following manner –

**VALUE OF PERQUISITE PER CALENDAR MONTH**

Sl. No.	Circumstances	Where cubic capacity of engine does not exceed 1.6 litres	Where cubic capacity of engine exceeds 1.6 litres
(1)	(2)	(3)	(4)
(1)	Where the motor car is owned or hired by the employer and -  (a) <u>is used wholly and exclusively in the performance of his official duties</u>	Not a perquisite, provided the documents specified in Note (2) below the table are maintained by the employer.	Not a perquisite, provided the documents specified in Note (2) below the table are maintained by the employer.

	<p>(b) <u>is used exclusively for the private or personal purposes</u> of the employee or any member of his household and the running and maintenance <u>expenses are met or reimbursed by the employer;</u></p> <p>(c) <u>is used partly in the performance of duties and partly for private or personal purposes</u> of his own or any member of his household and -</p> <p>(i) the expenses on maintenance and running are met or reimbursed by the employer</p> <p>(ii) the expenses on running and maintenance for private or personal use are fully met by the assessee.</p>	<p>Actual amount of expenditure incurred by the employer on the running and maintenance of motor car during the relevant previous year including remuneration, if any, paid by the employer to the chauffeur as increased by the amount representing normal wear and tear of the motor car and as reduced by any amount charged from the employee for such use.</p> <p>₹ 1,800 (plus ₹ 900, if chauffeur is also provided to run the motor car)</p> <p>₹ 600 (plus ₹ 900, if chauffeur is also provided by the employer to run the motor car)</p>	<p>Actual amount of expenditure incurred by the employer on the running and maintenance of motor car during the relevant previous year including remuneration, if any, paid by the employer to the chauffeur as increased by the amount representing normal wear and tear of the motor car and as reduced by any amount charged from the employee for such use.</p> <p>₹ 2,400 (plus ₹ 900, if chauffeur is also provided to run the motor car)</p> <p>₹ 900 (plus ₹ 900, if chauffeur is also provided by the employer to run the motor car)</p>
(2)	<p><u>Where the employee owns a motor car</u> but the actual running and maintenance charges (including remuneration of the chauffeur, if any) are met or reimbursed to him by the employer and</p> <p>(a) such reimbursement is</p>	<p>Not a perquisite, provided the documents specified in Note (2)</p>	<p>Not a perquisite, provided the documents specified in</p>

	<p><u>for the use of the vehicle wholly and exclusively for official purposes</u></p> <p>(b) such reimbursement is <u>for the use of the vehicle partly for official purposes and partly for personal or private purposes of the employee or any member of his household.</u></p>	<p>below the table are maintained by the employer.</p> <p>The actual amount of expenditure incurred by the employer</p> <p><b>as reduced by</b></p> <p>the amount specified in Sl. No. (1)(c)(i) above.</p> <p>(Also see note (2) below this table).</p>	<p>Note (2) below the table are maintained by the employer.</p> <p>The actual amount of expenditure incurred by the employer</p> <p><b>as reduced by</b></p> <p>the amount specified in Sl. No. (1)(c)(i) above.</p> <p>(Also see note (2) below this table).</p>
(3)	<p><b>Where the employee owns any other automotive conveyance</b> but the actual running and maintenance charges are met or reimbursed to him by the employer and</p> <p>(a) such reimbursement is for the use of the vehicle wholly and exclusively for official purposes</p> <p>(b) such reimbursement is for the use of vehicle partly for official purposes and partly for personal or private purposes of the employee</p>	<p>Not a perquisite, provided the documents specified in the note (2) below the table are maintained by the employer.</p> <p>The actual amount of expenditure incurred by the employer</p> <p><b>as reduced by</b></p> <p>the amount of ₹ 900.</p> <p>(Also see note (2) below the table)</p>	<p>Not applicable.</p>

**Notes:**

- (1) **Where more than one motor car is provided** - Where one or more motor-cars are owned or hired by the employer and the employee or any member of his household are allowed the use of such motor-car or all of any of such motor-cars (otherwise than wholly and exclusively in the performance of his duties), the value of perquisite shall be the amount

calculated in respect of one car as if the employee had been provided one motor-car for use partly in the performance of his duties and partly for his private or personal purposes and the amount calculated in respect of the other car or cars as if he had been provided with such car or cars exclusively for his private or personal purposes.

- (2) **Documents to be maintained in certain cases** - Where the employer or the employee claims that the motor-car is used wholly and exclusively in the performance of official duty or that the actual expenses on the running and maintenance of the motor-car owned by the employee for official purposes is more than the amounts deductible in Sl. No. 2(b) or 3(b) of the above table, he may claim a higher amount attributable to such official use and the value of perquisite in such a case shall be the actual amount of charges met or reimbursed by the employer as reduced by such higher amount attributable to official use of the vehicle provided that the following conditions are fulfilled :-
- (a) the employer has maintained complete details of journey undertaken for official purpose which may include date of journey, destination, mileage, and the amount of expenditure incurred thereon;
  - (b) the employer gives a certificate to the effect that the expenditure was incurred wholly and exclusively for the performance of official duties.
- (3) **Meaning of Normal wear and tear of a motor-car** - For computing the perquisite value of motor car, the normal wear and tear of a motor-car shall be taken at 10% per annum of the actual cost of the motor-car or cars.

**(D) Valuation of benefit of provision of domestic servants [Sub-rule (3) of Rule 3]**

If servants are engaged by the employee and employer paid or reimbursed the employee for the wages of such servants, it will be perquisite in the hands of all employees. But if the domestic servants are engaged by the employer and facility of such servants is provided to the employee, it will be perquisite in the hands of specified employees only.

- (i) The value of benefit to the employee or any member of his household resulting from the provision by the employer of the services of a sweeper, a gardener, a watchman or a personal attendant, shall be the actual cost to the employer.
- (ii) The actual cost in such a case shall be 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.

**ILLUSTRATION 21**

*Mr. Ram and Mr. Shyam are working for M/s. Alpha Ltd. As per salary fixation norms, the following perquisites were offered:*

- (i) *For Mr. Ram, who engaged a domestic servant for ₹ 1,000 per month, his employer reimbursed the entire salary paid to the domestic servant i.e. ₹ 1,000 per month.*

- (ii) For Mr. Shyam, he was provided with a domestic servant @ ₹ 1,000 per month as part of remuneration package.

You are required to comment on the taxability of the above in the hands of Mr. Ram and Mr. Shyam, who are not specified employees.

### SOLUTION

In the case of Mr. Ram, the domestic servant is engaged by the employee. Hence, his salary becomes an obligation which the employee would have discharged even if the employer did not reimburse the same. Such obligations of the employee borne by the employer are perquisite covered under section 17(2)(iv). It is taxable in the case of all employees (specified or non-specified) and hence a sum of ₹ 1000 p.m. would be taxed as perquisite in the hands of Mr. Ram.

In the case of Mr. Shyam, the domestic servant is not engaged by the employee but is provided by the employer. Thus, it cannot be considered as an obligation which the employee is required to meet. The employee might choose not to have a domestic servant. Such benefits or amenities are taxable as perquisite under section 17(2)(iii), only in the case of specified employees. Since, Mr. Shyam is not a specified employee there is no perquisite taxable in his hands.

#### **(E) Valuation of gas, electricity or water supplied by employer [Sub-rule (4) of Rule 3]**

If gas, electricity or water connections are taken by the employee and employer paid or reimbursed the employee for such expenses, it will be perquisite in the hands of all employees. But if the gas, electricity or water connections are taken in the name of employer and facility of such supplies are provided to the employee, it will be perquisite in the hands of specified employees only. The value of benefit to the employee resulting from the provision of gas, electricity or water supplied by the employer shall be determined as follow:

Circumstances	Value of benefit
If payment is made to agency supplying of gas, electricity etc.	sum equal to the amount paid on that account by the employer to the agency supplying the gas, electric energy or water
If supply is made from resources owned by the employer	manufacturing cost per unit incurred by the employer

Where the employee is paying any amount in respect of such services, the amount so paid shall be deducted from the value so arrived at.

#### **(F) Valuation of free or concessional educational facilities [Sub-rule (5) of Rule 3]**

If school fees of children of employee or any member of employee's household is paid or reimbursed by the employer on employee's behalf, it will be perquisite in the hands of all employees. But if the education facility is provided in the school maintained by the employer or in any school by reason of his being employment at free of cost or at concessional rate, it would be

perquisite in the hands of specified employees only. The value of benefit to the employee resulting from the provision of free or concessional educational facility for any member of his household shall be determined as follow:

Circumstances	Value of benefit
If the educational institution is maintained and owned by the employer	cost of such education in a similar institution in or near the locality. However, there would be no perquisite if the cost of such education or the value of such <b>benefit per child</b> does not exceed ₹ 1,000 p.m.
If free educational facilities are allowed in any other educational institution by reason of his being in employment of that employer	
Others	amount of expenditure incurred by the employer in that behalf

Where any amount is paid or recovered from the employee on that account, the value of benefit shall be reduced by the amount so paid or recovered.

**Note:** The exemption of ₹ 1,000 p.m. is allowed only in case of education facility provided to the children of the employee not in case of education facility provided to other household members.

**(G) Free or concessional tickets [Sub-rule (6) of Rule 3]**

The value of any benefit or amenity resulting from the provision by an employer

- who is engaged in the carriage of passengers or goods,
- to any employee or to any member of his household for personal or private journey free of cost or at concessional fare,
- in any conveyance owned, leased or made available by any other arrangement by such employer for the purpose of transport of passengers or goods

shall be taken to be the value at which such benefit or amenity is offered by such employer to the public as reduced by the amount, if any, paid by or recovered from the employee for such benefit or amenity.

However, there would be no such perquisite to the employees of an airline or the railways.

**(H) Valuation of other fringe benefits and amenities [Sub-rule (7) of Rule 3]**

Section 17(2)(viii) provides that the value of any other fringe benefit or amenity as may be prescribed would be included in the definition of perquisite and taxable in the hands of all employees. Accordingly, the following other fringe benefits or amenities are prescribed and the value thereof shall be determined in the manner provided hereunder:-

(i) **Interest-free or concessional loan [Sub-rule 7(i) of Rule 3]**

- (a) The value of the benefit to the assessee resulting from the provision of interest-free or concessional loan for any purpose made available to

- the employee or
- any member of his household

during the relevant previous year by the employer or any person on his behalf shall be determined as the sum equal to the interest computed at the rate charged per annum by the State Bank of India, as on the 1<sup>st</sup> day of the relevant previous year in respect of loans for the same purpose advanced by it on the maximum outstanding monthly balance as reduced by the interest, if any, actually paid by him or any such member of his household.

**“Maximum outstanding monthly balance”** means the aggregate outstanding balance for each loan as on the last day of each month.

- (b) However, **no value would be charged** if such loans are made available for medical treatment in respect of prescribed diseases (like cancer, tuberculosis, etc.) or where the amount of loans are **not exceeding in the aggregate ₹ 20,000**.
- (c) Further, where the benefit relates to the loans made available for medical treatment referred to above, the exemption so provided shall not apply to so much of the loan as has been reimbursed to the employee under any medical insurance scheme.

**ILLUSTRATION 22**

*Ranjit has taken an interest-free loan of ₹ 10 lakhs from his company. The amount is utilized by him for purchasing a house on 30-06-2020. The house is self-occupied. As per the scheme of the company, loan would be recovered in 40 equal monthly instalments recoverable immediately after the completion of 18<sup>th</sup> month from the date of purchase. Assuming the SBI lending rate of similar loan on 1.4.2021 was 9.75%. Calculate the perquisite value of such loan in the hands of Ranjit for the assessment year 2022-23. Is it possible to get deduction of perquisite value of interest under section 24(b)? Does it make any difference, if the house is given on rent?*

**SOLUTION**

First instalment will be due on 1<sup>st</sup> January, 2022. Amount of instalment will be:

$$₹ 10,00,000 \div 40 = ₹ 25,000.$$

Therefore, value for perquisite for interest-free loan will be calculated by applying the interest rate charged by the State Bank of India on the first day of the relevant previous year, on the outstanding amount of loan as reduced by the interest, if any, actually paid by the employee. Therefore, the value of perquisite will be as follows:

		₹
From April 21 to Dec. 21	(₹ 10,00,000 x 9.75% x 9/12)	73,125
For the month of Jan. 22	(₹ 9,75,000 x 9.75% x 1/12)	7,922
For the month of Feb. 22	(₹ 9,50,000 x 9.75% x 1/12)	7,719
For the month of Mar. 22	(₹ 9,25,000 x 9.75% x 1/12)	7,516
<b>Total</b>		<b>96,282</b>

Therefore, the perquisite value of interest-free loan will be ₹ 96,282.

The deduction for interest on capital borrowed for the purchase, construction, re-construction, repair or renewals of house property is available under section 24(b) only if such interest is actually payable. In this case, Mr. Ranjit is provided with an interest-free loan i.e. no interest is actually payable on the amount of loan. Thus, the value of perquisite of ₹ 96,282 cannot be claimed as deduction under section 24(b). The deduction of the value of perquisite shall not be available under 24(b), whether the house is self-occupied or let out.

(ii) **Travelling, touring and accommodation [Sub-rule 7(ii) of Rule 3]**

- (a) **If Travelling, touring, accommodation etc. expenses are paid or reimbursed by employer** - The value of travelling, touring, accommodation and any other expenses paid for or borne or reimbursed by the employer for any holiday availed of by the employee or any member of his household, other than leave travel concession or assistance, shall be determined as the sum equal to the amount of the expenditure incurred by such employer in that behalf.
- (b) **If Travelling, touring, accommodation etc. facilities are maintained by employer to particular employees only** - Where such facility is maintained by the employer, and is not available uniformly to all employees, the value of benefit shall be taken to be the value at which such facilities are offered by other agencies to the public.
- (c) **Expenses on any member of household accompanying such employee on office tour** - Where the employee is on official tour and the expenses are incurred in respect of any member of his household accompanying him, the amount of expenditure so incurred shall also be a fringe benefit or amenity.
- (d) **If official tour is extended as vacation** - However, where any official tour is extended as a vacation, the value of such fringe benefit shall be limited to the expenses incurred in relation to such extended period of stay or vacation. The amount so determined shall be reduced by the amount, if any, paid or recovered from the employee for such benefit or amenity.



(iii) **Free or concessional food and non-alcoholic beverages [Sub-rule 7(iii) of Rule 3]**

- (a) The value of free food and non-alcoholic beverages provided by the employer to an employee shall be the amount of expenditure incurred by such employer. The amount so determined shall be reduced by the amount, if any, paid or recovered from the employee for such benefit or amenity:
- (b) However, the following would not be treated as a perquisite -
- (1) free food and non-alcoholic beverages provided by such employer during
    - working hours at office or business premises or
    - through paid vouchers which are not transferable and usable only at eating joints (exemption would not be available in case of an employee, being an assessee, who opts for the provisions of section 115BAC),to the extent the value thereof either case does not exceed **fifty rupees per meal** or
  - (2) tea or snacks provided during working hours or
  - (3) free food and non-alcoholic beverages during working hours provided in a remote area or an off-shore installation.

(iv) **Value of gift, voucher or token in lieu of such gift [Sub-rule 7(iv) of Rule 3]**

- (a) The value of any gift, or voucher, or token in lieu of which such gift may be received by the employee or by member of his household on ceremonial occasions or otherwise from the employer shall be determined as the sum equal to the amount of such gift:
- (b) However, if the value of such gift, voucher or token, as the case may be, **is below ₹ 5,000** in the aggregate during the previous year, the value of perquisite shall be taken as 'Nil'.

(v) **Credit card expenses [Sub-rule 7(v) of Rule 3]**

- (a) The amount of expenses including membership fees and annual fees incurred by the employee or any member of his household, which is charged to a credit card (including any add-on-card) provided by the employer, or otherwise, paid for or reimbursed by such employer shall be taken to be the value of perquisite chargeable to tax as reduced by the amount, if any paid or recovered from the employee for such benefit or amenity.
- (b) However, such expenses incurred wholly and exclusively for official purposes would not be treated as a perquisite if the following conditions are fulfilled.

- (1) complete details in respect of such expenditure are maintained by the employer which may, *inter alia*, include the date of expenditure and the nature of expenditure;
- (2) the employer gives a certificate for such expenditure to the effect that the same was incurred wholly and exclusively for the performance of official duties.

**(vi) Club expenditure [Sub-rule 7(vi) of Rule 3]**

- (a) The value of benefit to the employee resulting from the payment or reimbursement by the employer of any expenditure incurred (including the amount of annual or periodical fee) in a club by him or by a member of his household shall be determined to be the actual amount of expenditure incurred or reimbursed by such employer on that account. The amount so determined shall be reduced by the amount, if any, paid or recovered from the employee for such benefit or amenity.

However, where the employer has obtained corporate membership of the club and the facility is enjoyed by the employee or any member of his household, the value of perquisite shall not include the initial fee paid for acquiring such corporate membership.

- (b) Further, if such expenditure is incurred wholly and exclusively for business purposes, it would not be treated as a perquisite provided the following conditions are fulfilled:-
  - (1) complete details in respect of such expenditure are maintained by the employer which may, *inter alia*, include the date of expenditure, the nature of expenditure and its business expediency;
  - (2) the employer gives a certificate for such expenditure to the effect that the same was incurred wholly and exclusively for the performance of official duties.
- (c) There would be no perquisite for use of health club, sports and similar facilities provided uniformly to all employees by the employer.

**(vii) Use of moveable assets [Sub-rule 7(vii) of Rule 3]**

Value of perquisite is determined as under:

Asset given	Value of benefit
(a) Use of laptops and computers	Nil
(b) Movable assets, other than - (i) laptops and computers; and (ii) assets already specified	10% p.a. of the actual cost of such asset, <b>or</b> the amount of rent or charge paid, or payable by the employer, <b>as the case may be</b>

**Note:** Where the employee is paying any amount in respect of such asset, the amount so paid shall be deducted from the value of perquisite determined above.

**(viii) Transfer of moveable assets [Sub-rule 7(viii) of Rule 3]**

Value of perquisite is determined as under:

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]

**Note:** Where the employee is paying any amount in respect of such asset, the amount so paid shall be deducted from the value of perquisite determined above.

**ILLUSTRATION 23**

Find out the taxable value of perquisite from the following particulars in case of an employee to whom the following assets held by the company were sold on 13.6.2021:

	Car	Laptop	Furniture
Cost of Purchase (May 2019) (₹)	8,72,000	1,22,500	35,000
Sale Price (₹)	5,15,000	25,000	10,000

The assets were put to use by the company from the day these were purchased.

**SOLUTION**

The assets transferred by the company shall be considered for the purpose of valuation of perquisites under section 17(2) read with 3(7)(viii). The value of perquisite in respect of assets transferred is determined after allowing normal wear & tear for the period of use of such assets by employer.

	Car	Laptop	Furniture
Rate of Depreciation	20%	50%	10%
Basis of Depreciation	WDV	WDV	SLM
Cost of asset to company – May 2019	8,72,000	1,22,500	35,000
Less: Normal wear & tear upto May, 2020	1,74,400	61,250	3,500
	6,97,600	61,250	31,500
Less: Normal wear and tear upto May, 2021	1,39,520	30,625	3,500
Balance, in May, 2021	5,58,080	30,625	28,000
Less: Sale value on 13.06.2021	5,15,000	25,000	10,000
<b>Value of Perquisite</b>	<b>43,080</b>	<b>5,625</b>	<b>18,000</b>

**Note:** As per Rule 3(7) of Income-tax Rules, 1962 normal wear and tear has to be calculated at the aforementioned prescribed rates applying Straight Line Method (SLM) to Furniture and Written Down Value (WDV) method to Laptop and Car.

(ix) **Other benefit or amenity [Sub-rule 7(ix) of Rule 3]**

The value of any other benefit or amenity, service, right or privilege provided by the employer shall be determined on the basis of cost to the employer under an arms' length transaction as reduced by the employee's contribution, if any.

However, there will be **no taxable perquisite in respect of expenses on telephones including mobile phone** actually incurred on behalf of the employee by the employer i.e., if an employer pays or reimburses telephone bills or mobile phone charges of employee, there will be no taxable perquisite.

(i) **Valuation of specified security or sweat equity share for the purpose of section 17(2)(vi) [Sub-rule (8) of Rule 3]**

The fair market value of any specified security or sweat equity share, being an equity share in a company, on the date on which the option is exercised by the employee, shall be determined in the following manner -

- (i) **If shares are listed on recognized stock exchange** - In a case where, on the date of the exercising of the option, the share in the company is listed on a recognized stock exchange, the fair market value shall be the average of the opening price and closing price of the share on that date on the said stock exchange.

**If shares are listed on more than one recognized stock exchange** - Where, on the date of exercising of the option, the share is listed on more than one recognized stock exchanges, the fair market value shall be the average of opening price and closing price of the share on the recognised stock exchange which records the highest volume of trading in the share.

**If no trading in share on recognized stock exchange** - Where on the date of exercising of the option, there is no trading in the share on any recognized stock exchange, the fair market value shall be—

- (a) the closing price of the share on any recognised stock exchange on a date closest to the date of exercising of the option and immediately preceding such date; or
- (b) the closing price of the share on a recognised stock exchange, which records the highest volume of trading in such share, if the closing price, as on the date closest to the date of exercising of the option and immediately preceding such date, is recorded on more than one recognized stock exchange.

**“Closing price”** of a share on a recognised stock exchange on a date shall be the price of the last settlement on such date on such stock exchange.

However, where the stock exchange quotes both “buy” and “sell” prices, the closing price shall be the “sell” price of the last settlement.

“**Opening price**” of a share on a recognised stock exchange on a date shall be the price of the first settlement on such date on such stock exchange.

However, where the stock exchange quotes both “buy” and “sell” prices, the opening price shall be the “sell” price of the first settlement.

- (ii) **If shares are not listed on recognized stock exchange** - In a case where, on the date of exercising of the option, the share in the company is not listed on a recognised stock exchange, the fair market value shall be such value of the share in the company as determined by a merchant banker on the specified date.

For this purpose, “**specified date**” means, —

- (a) the date of exercising of the option; or
- (b) any date earlier than the date of the exercising of the option, not being a date which is more than 180 days earlier than the date of the exercising.

**Note:** Where any amount has been recovered from the employee, the same shall be deducted to arrive at the value of perquisites.

**(J) Valuation of specified security not being an equity share in a company for the purpose of section 17(2)(vi) [Sub-rule (9) of Rule 3]**

The fair market value of any specified security, not being an equity share in a company, on the date on which the option is exercised by the employee, shall be such value as determined by a merchant banker on the specified date.

For this purpose, “**specified date**” means,—

- (i) the date of exercising of the option; or
- (ii) any date earlier than the date of the exercising of the option, not being a date which is more than 180 days earlier than the date of the exercising.

Tax on perquisite of specified securities and sweat equity shares is required to be paid in the year of exercising of option. However, where such shares or securities are allotted by the current employer, being an eligible start-up referred to in section 80-IAC, the perquisite is taxable in the year

- after the expiry of 48 months from the end of the relevant assessment year
  - in which sale of such security or share are made by the assessee
  - in which the assessee ceases to be the employee of the employer,
- whichever is earlier.

### Definitions for the purpose of perquisite rules -

The following definitions are relevant for applying the perquisite valuation rules -

Term	Meaning
<b>Member of household</b>	shall <b>include</b> - (a) spouse(s), (b) children and their spouses, (c) parents, and (d) servants and dependants;
<b>Salary</b>	<b>includes</b> the pay, allowances, bonus or commission payable monthly or otherwise or any monetary payment, by whatever name called from one or more employers, as the case may be, <b>but does not include</b> the following, namely: - (a) dearness allowance or dearness pay unless it enters into the computation of superannuation or retirement benefits of the employee concerned; (b) employer's contribution to the provident fund account of the employee; (c) allowances which are exempted from payment of tax; (d) the value of perquisites specified in section 17(2); (e) any payment or expenditure specifically excluded under proviso to section 17(2); (f) lump-sum payments received at the time of termination of service or superannuation or voluntary retirement, like gratuity, severance pay, leave encashment, voluntary retrenchment benefits, commutation of pension and similar payments;

### ILLUSTRATION 24

*X Ltd. provided the following perquisites to its employee Mr. Y for the P.Y.2021-22 –*

- (1) *Accommodation taken on lease by X Ltd. for ₹ 20,000 p.m. ₹ 10,000 p.m. is recovered from the salary of Mr. Y.*
- (2) *Furniture, for which the hire charges paid by X Ltd. is ₹ 5,000 p.m. No amount is recovered from the employee in respect of the same.*
- (3) *An motor car with 1.2 litres cubic capacity which is owned by X Ltd. and is given to Mr. Y to be used both for official and personal purposes. All running and maintenance expenses are fully met by the employer. He is also provided with a chauffeur.*
- (4) *A gift voucher of ₹ 15,000 on his birthday.*

*Compute the value of perquisites chargeable to tax for the A.Y.2022-23, assuming his salary for perquisite valuation to be ₹ 10 lakh.*

**SOLUTION**

**Computation of the value of perquisites chargeable to tax in the hands of Mr. Y for the A.Y.2022-23**

	Particulars	Amount in ₹		
(1)	<b>Value of concessional accommodation</b>			
	Actual amount of lease rental paid by X Ltd.	2,40,000		
	15% of salary i.e., 15% of ₹ 10,00,000	1,50,000		
	Lower of the above		1,50,000	
	Less: Rent paid by Mr. Y (₹ 10,000 × 12)		1,20,000	
			30,000	
	Add: Hire charges paid by X Ltd. for furniture provided for the use of Mr. Y (₹ 5,000 × 12)		60,000	90,000
(2)	Perquisite value of motor car owned by X Ltd. and provided to Mr. Y for his personal and official use [(₹ 1,800 + ₹ 900) × 12]			32,400
(3)	Value of gift voucher*			15,000
	<b>Value of perquisites chargeable to tax</b>			<b>1,37,400</b>
* An alternate view possible is that only the sum in excess of ₹ 5,000 is taxable. In such a case, the value of perquisite would be ₹ 10,000				



## 4.4 DEDUCTIONS FROM SALARY

The income chargeable under the head 'Salaries' is computed after making the following deductions:

- (1) Standard deduction [Section 16(ia)]
- (2) Entertainment allowance [Section 16(ii)]
- (3) Professional tax [Section 16(iii)]

### (1) Standard deduction

A standard deduction of ₹ 50,000 or the amount of salary, whichever is lower, is to be provided to the employees.

### (2) Entertainment allowance

Entertainment allowance received is fully taxable and is first to be included in the salary and thereafter the following deduction is to be made from gross salary:

However, deduction in respect of entertainment allowance is available in case of Government employees only. The amount of deduction will be lower of:

- (i) One-fifth of his basic salary or
- (ii) ₹ 5,000 or
- (iii) Entertainment allowance received.

Amount actually spent by the employee towards entertainment out of the entertainment allowance received by him is not a relevant consideration at all.

### (3) Professional tax on employment

Professional tax or taxes on employment levied by a State under Article 276 of the Constitution is allowed as deduction only when it is actually paid by the employee during the previous year. The total amount by way of professional tax payable in respect of any one person shall not exceed ₹ 2,500 per annum. However, the amount paid during the previous year can be more than ₹ 2,500 as the employee may have paid the professional tax of an earlier year during the previous year.

If professional tax is reimbursed or directly paid by the employer on behalf of the employee, the amount so paid is first included as salary income and then allowed as a deduction u/s 16.

#### ILLUSTRATION 25

*Mr. Gupta receives the following emoluments during the previous year ending 31.03.2022.*

<i>Basic pay</i>	<i>₹ 50,000</i>
<i>Dearness Allowance</i>	<i>₹ 15,000</i>
<i>Commission</i>	<i>₹ 15,000</i>
<i>Entertainment allowance</i>	<i>₹ 5,000</i>
<i>Medical expenses reimbursed</i>	<i>₹ 20,000</i>
<i>Professional tax paid</i>	<i>₹ 2,000 (₹ 1,000 was paid by his employer)</i>

*Mr. Gupta contributes ₹ 7,000 towards recognized provident fund. He has no other income. Determine the income from salary for A.Y. 2022-23, if Mr. Gupta is a State Government employee.*

#### SOLUTION

##### Computation of salary of Mr. Gupta for the A.Y.2022-23

Particulars	₹	₹
Basic Salary		50,000
Dearness Allowance		15,000
Commission		15,000



Entertainment Allowance received		5,000
Employee's contribution to RPF [Note]		-
Medical expenses reimbursed		20,000
Professional tax paid by the employer		1,000
<b>Gross Salary</b>		<b>1,06,000</b>
Less: Deductions under section 16		
under section 16(ia) - Standard deduction of upto ₹ 50,000		50,000
under section 16(ii) - Entertainment allowance being lower of:		
(a) Allowance received	5,000	
(b) One fifth of basic salary [ $1/5 \times ₹ 50,000$ ]	10,000	
(c) Statutory amount	5,000	5,000
under section 16(iii) Professional tax paid		2,000
<b>Income from Salary</b>		<b>49,000</b>

**Note:** Employee's contribution to RPF is not taxable. It is eligible for deduction u/s 80C.



## 4.5 RELIEF UNDER SECTION 89

- (1) **On account of arrears of salary or advance salary:** Where by reason of any portion of an assessee's salary being paid in arrears or in advance or by reason of his having received in any one financial year, salary for more than twelve months or a payment of profit in lieu of salary under section 17(3), his income is assessed at a rate higher than that at which it would otherwise have been assessed, the Assessing Officer shall, on an application made to him in this behalf, grant such relief as prescribed. The procedure for computing the relief is given in Rule 21A.
- (2) **On account of family pension:** Similar tax relief is extended to assessee who receive arrears of family pension as defined in the *Explanation* to clause (iia) of section 57.  
**"Family pension"** means a regular monthly amount payable by the employer to a person belonging to the family of an employee in the event of his death.
- (3) **No relief at the time of Voluntary retirement or termination of service:** No relief shall be granted in respect of any amount received or receivable by an assessee on his voluntary retirement or termination of his service, in accordance with any scheme or schemes of voluntary retirement or a scheme of voluntary separation (in the case of a public sector company), if exemption under section 10(10C) in respect of such compensation received on voluntary retirement or termination of his service or voluntary separation has been claimed by the assessee in respect of the same assessment year or any other assessment year.

**ILLUSTRATION 26**

In the case of Mr. Harry, who turned 69 years on 28.3.2022, you are informed that the salary for the previous year 2021-22 is ₹ 11,20,000 (computed) and arrears of salary received is ₹ 4,50,000. Further, you are given the following details relating to the earlier years to which the arrears of salary received is attributable to:

Previous Year	Taxable Salary	Arrears now received (₹)
2010 – 2011	8,00,000	1,50,000
2011 – 2012	8,75,000	1,25,000
2012 – 2013	9,00,000	1,75,000

Compute the relief available under section 89 and the tax payable for the A.Y. 2022-23. Assume that Mr. Harry does not opt for section 115BAC.

**Note: Rates of Taxes:**

Assessment Year	Slab rates of income-tax			
	For resident individuals of the age of 60 years or more at any time during the previous year		For other resident individuals	
	Slabs	Rate	Slabs	Rate
2011-12	Upto ₹ 2,40,000	Nil	Upto ₹ 1,60,000	Nil
	₹ 2,40,000 - ₹ 5,00,000	10%	₹ 1,60,000 - ₹ 5,00,000	10%
	₹ 5,00,000 - ₹ 8,00,000	20%	₹ 5,00,000 - ₹ 8,00,000	20%
	Above ₹ 8,00,000	30%	Above ₹ 8,00,000	30%
2012-13	Upto ₹ 2,50,000	Nil	Upto ₹ 1,80,000	Nil
	₹ 2,50,000 - ₹ 5,00,000	10%	₹ 1,80,000 - ₹ 5,00,000	10%
	₹ 5,00,000 - ₹ 8,00,000	20%	₹ 5,00,000 - ₹ 8,00,000	20%
	Above ₹ 8,00,000	30%	Above ₹ 8,00,000	30%
2013-14	Upto ₹ 2,50,000	Nil	Upto ₹ 2,00,000	Nil
	₹ 2,50,000 - ₹ 5,00,000	10%	₹ 2,00,000 - ₹ 5,00,000	10%
	₹ 5,00,000 - ₹ 10,00,000	20%	₹ 5,00,000 - ₹ 10,00,000	20%
	Above ₹ 10,00,000	30%	Above ₹ 10,00,000	30%

**Note** – Education cess@2% and secondary and higher education cess@1% was attracted on the income-tax for all above preceding years.

**SOLUTION****Computation of tax payable by Mr. Harry for the A.Y.2022-23**

Particulars	Incl. arrears of salary ₹	Excl. arrears of salary ₹
Current year salary (computed)	11,20,000	11,20,000
Add: Arrears of salary	4,50,000	
Taxable Salary	15,70,000	11,20,000
Income-tax thereon	2,81,000	1,46,000
Add: Health & Education cess@4 %	11,240	5,840
<b>Total payable</b>	<b>2,92,240</b>	<b>1,51,840</b>

**Computation of tax payable on arrears of salary if charged to tax in the respective AYs**

Particulars	A.Y. 2011-12		A.Y. 2012-13		A.Y. 2013-14	
	Incl. arrears ₹	Excl. arrears ₹	Incl. arrears ₹	Excl. arrears ₹	Incl. arrears ₹	Excl. arrears ₹
Taxable salary	8,00,000	8,00,000	8,75,000	8,75,000	9,00,000	9,00,000
Add: Arrears of salary	1,50,000	-	1,25,000	---	1,75,000	---
<b>Taxable salary</b>	<b>9,50,000</b>	<b>8,00,000</b>	<b>10,00,000</b>	<b>8,75,000</b>	<b>10,75,000</b>	<b>9,00,000</b>
Tax on the above	1,39,000	94,000	1,52,000	1,14,500	1,47,500	1,05,000
Add: Cess@3%	4,170	2,820	4,560	3,435	4,425	3,150
<b>Tax payable</b>	<b>1,43,170</b>	<b>96,820</b>	<b>1,56,560</b>	<b>1,17,935</b>	<b>1,51,925</b>	<b>1,08,150</b>

**Computation of relief under section 89**

	Particulars	₹	₹
(i)	Tax payable in A.Y.2022-23 on arrears:		
	Tax on income including arrears	2,92,240	
	Less : Tax on income excluding arrears	1,51,840	1,40,400
(ii)	Tax payable in respective years on arrears:		
	Tax on income incl. arrears (₹ 1,43,170 + ₹ 1,56,560 + ₹ 1,51,925)	4,51,655	
	Less: Tax on income excluding arrears (₹ 96,820 + ₹ 1,17,935 + ₹ 1,08,150)	3,22,905	1,28,750
	Relief under section 89 - difference between tax on arrears in A.Y 2022-23 and tax on arrears in the respective years		<b>11,650</b>

**Tax payable for A.Y.2022-23 after relief under section 89**

Particulars	₹
Income-tax payable on total income including arrears of salary	2,92,240
Less : Relief under section 89 as computed above	11,650
<b>Tax payable after claiming relief</b>	<b>2,80,590</b>

**4.6 SALARY FROM UNITED NATIONS ORGANISATION**

Section 2 of the United Nations (Privileges and Immunities) Act, 1947 grants exemption from income-tax to salaries and emoluments paid by the United Nations to its officials. Besides salary, any pension covered under the United Nations (Privileges and Immunities) Act and received from UNO is also exempt from tax.

## SIGNIFICANT SELECT CASES

S.No.	Case Law	
1.	<b><i>CIT v. Shankar Krishnan (2012) 349 ITR 0685 (Bom)</i></b>	
	<b>Issue</b>	<b>Decision</b>
	Can notional interest on security deposit given to the landlord in respect of residential premises taken on rent by the employer and provided to the employee, be included in the perquisite value of rent-free accommodation given to the employee?	The <b>notional interest on the security deposit given by the employer to the landlord cannot be included in valuation of the perquisite, since the perquisite value has to be computed as per Rule 3</b> ; and the said Rule does not require addition of such notional interest. Thus, the perquisite value of the residential accommodation provided by the employer would be the actual amount of lease rental paid or payable by the employer or 15% of salary, whichever is lower.
2.	<b><i>CIT (TDS) v. Director, Delhi Public School (2011) 202 Taxman 318 (Punj. &amp; Har.)</i></b>	
	<b>Issue</b>	<b>Decision</b>
	Can the limit of ₹ 1,000 per month per child be allowed as standard deduction, while computing the perquisite value of free or concessional education facility provided to the employee by the employer?	In case the value of perquisite for free/ concessional educational facility arising to an employee <b>exceeds ₹ 1,000 per month per child, the whole perquisite shall be taxable in the hands of the employee and no standard deduction of ₹ 1,000 per month per child can be provided from the same</b> . It is only in case the perquisite value is less than ₹ 1,000 per month per child, the perquisite value shall be nil. Therefore, ₹ 1,000 per month per child is not a standard deduction to be provided while calculating such a perquisite.

**TEST YOUR KNOWLEDGE****Question 1**

*Examine the correctness or otherwise of the following case in the context of provisions contained in the Income-tax Act, 1961 relevant/applicable for the assessment year 2022-23:*

- (i) *Nargis, working as Regional Area Sales Manager of Pincer Marketing Ltd., was paid salary and a commission based as a percentage on the volume of sales effected by her. Nargis claimed the expenses such as travelling, telephone, postage etc., incurred by her for earning the commission in the return of income, which were disallowed by the Assessing Officer.*
- (ii) *An amount of ₹ 12,50,000 paid by XYZ Ltd., after approval by the board, to a hospital in UK for the heart surgery of its managing director was charged under medical expenses. The Assessing Officer, while completing the assessment of the company, taxed the amount so paid by the company as a perquisite in the hands of its Managing Director.*

**Answer**

- (i) The facts of this case are similar to the case decided by the Madras High Court in *CIT v. R. Rajendran (2003) 260 ITR 0476*, where it was held that since the assessee was employed as a regional sales manager and the commission paid to him is based on the volume of sales effected, such commission was obviously paid to the employee as an encouragement to effect a higher level of sales. The commission paid in addition to what the employee was getting as a fixed salary would also constitute/ form part of salary. When the commission is chargeable as salary, then, no deduction is allowable in respect of any expenditure incurred to earn the commission.

Therefore, in this case, the claim made by Nargis is not valid and the expenses incurred for earning commission are not allowable as deduction while computing her salary income.

- (ii) A Managing Director generally occupies the dual capacity of being a director as well as an employee of the company. In this case, assuming that the Managing Director is also an employee of XYZ Ltd., clause (vi) of the proviso to section 17(2) would get attracted. Clause (vi) of the proviso to section 17(2) provides that any expenditure incurred by the employer on medical treatment of the employee outside India shall be excluded from perquisite only to the extent permitted by RBI. Therefore, the expenditure on medical treatment of the Managing Director outside India shall be excluded from perquisite to the extent permitted by RBI as per clause (vi) of the proviso to section 17(2). If it is assumed that the entire amount is permitted by RBI, there would be no perquisite chargeable in the hands of the Managing Director. Therefore, in such a case, the action of the Assessing Officer in taxing the entire amount paid by the company as a perquisite in the hands of the Managing Director is incorrect.

This question can also be answered by applying the rationale of the Allahabad High Court ruling in *CIT v. D.P. Kanodia (2008) 296 ITR 0616*. In that case, the High Court observed that the reimbursement by the company of medical expenditure incurred outside India by the director cannot be considered as an amenity or benefit provided by the company to its director, and therefore the provisions of section 17(2)(iii)(a) would not be attracted. Therefore, such reimbursement was not a perquisite within the meaning of section 17(2)(iii)(a).

Hence, applying the rationale of the above case to the facts of this case, the action of the Assessing Officer in taxing the amount paid by the company as a perquisite in the hands of the Managing Director is incorrect.

## Question 2

*Mr. X is a Member of Legislative Assembly. He underwent an open heart surgery abroad in respect of which he received ₹ 5 Lakhs from the State Government towards reimbursement of his medical expenses. The Assessing Officer contended that such amount is taxable as a perquisite under section 17. Examine the correctness of the contention of the Assessing Officer.*

## Answer

The facts of this case are similar to the facts in *CIT v. Shiv Charan Mathur (2008) 306 ITR 126 (Raj.)*. In the instant case, the High Court observed that MPs and MLAs do not fall within the meaning of “employees”. They are elected by the public, their election constituencies and it is consequent upon such election that they acquire constitutional position and are in charge of constitutional functions and obligations. The remuneration received by them, after swearing in, cannot be said to be salary within the meaning of section 15, since the basic ingredient of employer-employee relationship is missing in such cases.

Therefore, the remuneration received by MPs and MLAs is taxable under the head “Income from Other Sources” and not under the head “Salaries”. When the provisions of section 15 are not attracted to the remuneration received by MPs and MLAs, the provisions of section 17 also would not apply as section 17 only extends the definition of salary by providing that certain items mentioned therein would be included in salary as “perquisites”. Thus, reimbursement of medical expenditure (incurred for open heart surgery abroad) to an MLA cannot be taxed as a perquisite under section 17.

Applying the above ruling to the case on hand, the contention of the Assessing Officer is not correct.

## Question 3

*Mr. Kadam is entitled to a salary of ₹ 40,000 per month. He is given an option by his employer either to take house rent allowance or a rent free accommodation which is owned by the company. The HRA amount payable was ₹ 7,000 per month. The rent for the hired accommodation was ₹ 6,000 per month at New Delhi. Advise Mr. Kadam whether it would be beneficial for him to avail HRA or Rent Free Accommodation. Give your advice on the basis of “Net Take Home Cash benefits”. Assume Mr. Kadam does not opt for the provisions of section 115BAC.*

## Answer

## Computation of tax liability of Kadam under both the options

Particulars	Option I – HRA (₹)	Option II – RFA (₹)
Basic Salary (₹ 40,000 x 12 Months)	4,80,000	4,80,000
Perquisite value of rent-free accommodation (15% of ₹ 4,80,000)	N.A.	72,000
House rent Allowance (₹ 7,000 x 12 Months) ₹ 84,000		
Less: Exempt u/s 10(13A) – least of the following -		
- 50% of Basic Salary ₹ 2,40,000		
- Actual HRA received ₹ 84,000		
- Rent paid less 10% of salary ₹ 24,000 ₹ 24,000	60,000	
Gross Salary	5,40,000	5,52,000
Less: Standard deduction u/s 16(ia)	50,000	50,000
Net Salary	4,90,000	5,02,000
Less: Deduction under Chapter VI-A	-	-
<b>Total Income</b>	<b>4,90,000</b>	<b>5,02,000</b>
Tax on total income	12,000	12,900
Less: Rebate under section 87A - Lower of ₹ 12,500 or income-tax of ₹ 12,000, since total income does not exceed ₹ 5,00,000	12,000	Nil
	Nil	12,900
Add: Health and Education cess@4%	Nil	516
<b>Total tax payable</b>	<b>Nil</b>	<b>13,416</b>
<b>Tax Payable (Rounded off)</b>	<b>Nil</b>	<b>13,420</b>

## Cash Flow Statement

Particulars	Option I – HRA	Option II – RFA
Inflow: Salary	5,64,000	4,80,000
Less: Outflow: Rent paid	(72,000)	-
Tax on total income	Nil	(13,420)
<b>Net Inflow</b>	<b>4,92,000</b>	<b>4,66,580</b>

Since the net cash inflow under option I (HRA) is higher than in Option II (RFA), it is beneficial for Mr. Kadam to avail Option I, i.e., House Rent Allowance.



**Question 4**

*Mr. M is working with MNO Limited for the last 10 years. He was granted an option on 1.7.2019 by the company to purchase 800 equity shares at a price of ₹ 250 per share. The period during which the option can be exercised to purchase 800 shares at a pre-determined price of ₹ 250 per share commencing on 1.7.2019 and ending on 31.3.2021. Mr. M exercised the option on 15.3.2021 to purchase 500 shares. Fair market value on the said date was ₹ 6490 on the Bombay Stock Exchange and ₹ 6500 on the National Stock Exchange. The NSE has recorded the higher volume of trading in that share.*

*The company has allotted him 500 shares on 24th April, 2021. The fair market value on the date of allotment was ₹ 7100 per share on NSE and ₹ 7110 on the BSE that has recorded the higher volume of trading in that share. The option was granted for making available rights in the nature of intellectual property rights.*

*Determine the taxability of perquisite. Does it make any difference if the option was granted for providing technical know-how?*

**Answer**

The perquisite of sweat equity shares shall be taxable in the previous year 2021-22 (assessment year 2022-23), being the previous year of allotment of such shares. The value of sweat equity shares shall be the fair market value of such shares on the date on which the option is exercised by the assessee, as reduced by any amount actually paid by, or recovered from, the assessee in respect of such shares.

As per Rule 3(8) of the Income-tax Rules, 1962, the fair market value of a share on the date of exercising the option shall be the price of the share on the recognized stock exchange which records the highest volume of trading in such shares, in case the shares are listed on more than one recognised stock exchange.

Hence, the value of taxable perquisite for sweat equity shares

$$\begin{aligned}
 &= \text{FMV on the date of exercising the option on the NSE (since it recorded higher volume than BSE)} \quad (-) \quad \text{Amount recovered from the employee} \\
 &= (500 \times ₹ 6500) - (500 \times ₹ 250) \\
 &= ₹ 32,50,000 - ₹ 1,25,000 = ₹ 31,25,000
 \end{aligned}$$

As per section 17(2)(vi), "sweat equity shares" means equity shares issued by a company to its employees or directors at a discount or for consideration other than cash for providing technical knowhow or making available rights in the nature of intellectual property rights or value additions, by whatever name called.

Therefore, this provision is equally applicable whether the sweat equity shares option was granted for making available rights in the nature of intellectual property rights or for providing technical know-how.

**Question 5**

Ajay is employed as senior executive of Manu Ltd. Manu Ltd offers rights to its existing shareholders in the ratio 1:1 on 15<sup>th</sup> February 2022 at ₹ 150 per share.

Ajay was also offered 500 shares at ₹ 150, which he exercised. On these facts, you are consulted by Ajay as to:

- (a) The tax consequences for the assessment year 2022-23 assuming that fair market value on the date of exercise of option is ₹ 300.
- (b) If Ajay is already a shareholder of 500 shares, allotted in public issue will it make any difference?

**Answer**

- (a) As per section 17(2)(vi), 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 employee is taxable as perquisite. The meaning of the terms 'specified security', 'sweat equity shares', 'fair market value' are dealt with in the Explanation given therein.

The fair market value of the shares so determined in accordance with the method as may be prescribed less the amount actually recovered from the employee, shall be the value of perquisite chargeable to tax.

The value of perquisite would be:

	₹
Fair market value of shares determined as per the prescribed method in Income-tax Rules, 1962 = 500 shares @ ₹ 300 each	1,50,000
Less: Amount recovered from the employee @ ₹ 150 per share	75,000
<b>Value of perquisite chargeable to tax</b>	<b>75,000</b>

As per section 49(2AA), the cost of acquisition of specified security or sweat equity shares referred to in section 17(2)(vi) shall be the fair market value which has been taken into account for the purpose of perquisite valuation.

- (b) In case the employee is a shareholder and was allotted shares in the same manner as was allotted to other shareholders by the company without any concession/ reduction in value then the question of valuation of perquisite would not arise to the extent such shares are offered in capacity of a shareholder.