

Income Tax-I

Assessment Year 2018-19

For Bangalore University

(As per CBCS Syllabus 2014–15 as Revised in March 2017)

B.COM SEMESTER-V

About the Authors



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Dedicated to

Our Teachers, who taught us this subject

Our Students, who made us learn it better

Our Friends, who encouraged us to write this book



Preface

Tax is levied by every country on its citizens from time immemorial. Tax payment is inevitable and compulsory. It is considered a burden as the purpose and process of taxation is either not understood or misunderstood. Therefore, it is essential for every citizen to have a minimum knowledge and background of taxation and tax system in the country. This book makes an effort to have a simplified idea on the tax systems in the country—especially the **Income Tax**. This book is written keeping in mind the syllabus of Bangalore University, and hence does not cover the entire ambit of the subject. However, the topics covered are presented in a systematic and meticulous manner, hence providing the reader a strong foundation in the subject.

A thorough care has been taken to make the book error-free. Nonetheless, mistakes might have crept in inadvertently. We request our readers to bring to our notice, any such errors, omissions and mistakes, for enabling us to rectify in our future editions.

We thank **Dr. M. Ramachandra Gowda**, Registrar, Bangalore Central University and **Dr. K.N. Pushpalatha**, General Secretary, BSVP Trust, who have encouraged us and extended their support in carrying out this work.

We thank **Mr. Suman Sen** of Mc Graw Hill Education (India) for giving us the opportunity and constant encouragement in pursuing this project, **Ms. Shehla Mirza** for her innovative ideas and follow-ups to bring out the quality content, and **Mr. Piyaaray Pandita** for his excellent DTP and production work.

Our acknowledgements are also due to **Mrs. Meera Rajesh**, **Mrs. Savitha Sreekantha** and **Mr. Nischal**. This book could not be completed in time without their support and sacrifice.

Last but not the least, our acknowledgements are due to the **Almighty** who has blessed us with knowledge and given strength for spreading the same.

Dr. V. Rajesh Kumar
Dr. R. K. Sreekantha



Syllabus

Income Tax-I Bangalore University Semester-V

(As per CBCS Syllabus 2014–15 as Revised in March 2017)

5.3 Income Tax-I (Semester-V)	(IA-30 M + Written-70 M)	Chapter in the Book
Unit 1: INTRODUCTION TO INCOME TAX Brief History of Indian Income Tax—Legal Frame Work—Types of Taxes—Cannons of Taxation—Important Definitions: Assessment, Assessment Year, Previous Year (including Exceptions), Assessee, Person, Income, Casual Income, Gross Total Income, Agricultural Income (including Scheme of Partial Integration)—Scheme of taxation. Meaning and classification of Capital & Revenue. Income tax authorities: Powers & functions of CBDT, CIT & A.O. (Theory only).		Chapter 1, 2, 3, 6, 8, 11
Unit 2: EXEMPTED INCOMES Introduction—Exempted Incomes U/S 10—Restricted to Individual Assessee.		Chapter 7
Unit 3: RESIDENTIAL STATUS Residential Status of an Individual—Determination of Residential Status—Incidence of Tax—Problems		Chapter 4, 5
Unit 4: INCOME FROM SALARY Meaning—Definition—Basis of Charge—Advance Salary—Arrears of Salary—Allowances—Perquisites—Provident Fund—Profits in Lieu of Salary—Gratuity—Commutation of Pension—Encashment of Earned leave—Compensation for voluntary retirement—Deductions from Salary U/S 16—Problems on Income from Salary.		Chapter 9
Unit 5: INCOME FROM HOUSE PROPERTY Basis of Charge—Deemed Owners—Exempted Incomes from House Property—Composite Rent—Annual Value—Determination of Annual Value—Treatment of Unrealized Rent—Loss due to Vacancy—Deductions from Annual Value—Problems on Income from House Property.		Chapter 10

Skill Development

- Form No. 49A (PAN) and 49B.
- Filling of Income Tax Returns.
- List of enclosures to be made along with IT returns (with reference to salary & H.P).
- Preparation of Form 16.
- Computation of Income Tax and the Slab Rates.
- Computation of Gratuity.



Question Paper Pattern

Income Tax-I Semester-V

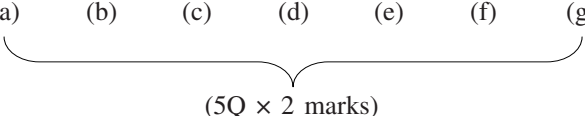
(As per CBCS Syllabus 2014–15 as Revised in March 2017)

Maximum Marks: 70

Duration: 03 Hours

Note:

1. Question paper consists of *three* sections-Section A, B and C
2. Question 1 carries *10 marks*.
3. Questions 2 to 6 each carries *6 marks*.
4. Questions 7 to 11 each carries *14 marks*.

Particulars	Marks	Nature of Question
SECTION-A (Conceptual Questions) Q-1: Answer any <i>five</i> sub questions out of <i>seven</i> (a) (b) (c) (d) (e) (f) (g)  (5Q × 2 marks)	10 marks	Theory
SECTION-B (Analytical Questions) Answer any <i>three</i> questions out of <i>five</i> Q-2 } Q-3 } Q-4 } (3 Q × 6 marks) Q-5 } Q-6 }	18 marks	Practical
SECTION-C (Essay Type Questions) Answer any <i>three</i> questions out of <i>five</i> Q-7 } Q-8 } Q-9 } (3 Q × 14 marks) Q-10 } Q-11 }	42 marks	Practical
Gross Total	70 Marks	



Contents

<i>About the Authors</i>	<i>ii</i>
<i>Preface</i>	<i>vii</i>
<i>Syllabus</i>	<i>ix</i>
<i>Question Paper Pattern</i>	<i>xi</i>
Chapter 1 Tax	1.1–1.8
1.1 Meaning of Tax 1.1	
1.2 Characteristics of Tax 1.1	
1.3 Classification of Tax 1.1	
1.4 Income Tax 1.2	
1.5 Importance of Income Tax 1.2	
1.6 Brief History of Income Tax 1.3	
1.7 Legal Framework of Income Tax in India 1.4	
1.7.1 The Finance Bill/Act 1.4	
1.8 Canons of Taxation 1.4	
1.9 Coverage or Scope of Income Tax Act, 1961 1.5	
1.10 Steps in ‘Assessment’ 1.6	
<i>Summary</i> 1.7	
<i>Theory Questions</i> 1.7	
Chapter 2 Assessee and Person	2.1–2.8
2.1 Assessee [Section 2(7)] 2.3	
2.2 Person [Section 2(31)] 2.4	
<i>Summary</i> 2.7	
<i>Theory Questions</i> 2.7	
<i>Exercises</i> 2.7	
Chapter 3 Assessment Year and Previous Year	3.1–3.7
3.1 Assessment Year [Section 2(9)] 3.3	
3.2 Previous Year [Section 3] 3.3	

3.3	General Rule of Previous Year and Exceptions to the Rule	3.4
	<i>Summary</i>	3.6
	<i>Theory Questions</i>	3.6
	<i>Exercises</i>	3.7
Chapter 4	Residential Status	4.1–4.21
4.1	Meaning and Introduction	4.3
4.2	Residential Status of Individual Assessee	4.3
	<i>Summary</i>	4.17
	<i>Theory Questions</i>	4.18
	<i>Exercises</i>	4.19
Chapter 5	Incidence of Tax	5.1–5.14
5.1	Meaning of Incidence of Tax	5.3
5.2	Requirements for Determining the Incomes of the Assessee that must be Considered	5.3
5.2.1	Indian Income	5.4
5.2.2	Foreign Income	5.5
5.3	Determination of the Incomes that must be Considered in Computing Taxable Income	5.5
	<i>Summary</i>	5.13
	<i>Theory Questions</i>	5.13
	<i>Exercises</i>	5.14
Chapter 6	Revenue and Capital Receipts	6.1–6.6
6.1	Meaning	6.3
6.2	Difference between Revenue Receipts and Capital Receipts	6.3
	<i>Summary</i>	6.6
	<i>Theory Questions</i>	6.6
	<i>Exercises</i>	6.6
Chapter 7	Exempted and Taxable Incomes	7.1–7.31
7.1	Introduction	7.3
7.2	Incomes Exempt under Section 10	7.4
7.3	Income Exempt under Section 10(1)	7.10
	<i>Summary</i>	7.26
	<i>Theory Questions</i>	7.26
	<i>Exercises</i>	7.27
Chapter 8	Heads of Income	8.1–8.17
8.1	Introduction	8.3
8.2	Chargeability under the head “Income from Salaries”	8.4

8.3	Chargeability under the head “Income from House Property”	8.4
8.4	Chargeability under the head “Income from Business or Profession”	8.6
8.5	Chargeability under the head “Capital Gains”	8.8
8.5.1	Capital Asset	8.8
8.5.2	Transfer	8.9
8.6	Chargeability under the head “Income From Other Sources”	8.12
<i>Summary</i>		8.16
<i>Theory Questions</i>		8.16
<i>Exercises</i>		8.17

Chapter 9 Computation of Taxable Income Under Each Head 9.1–9.140

9.1	Introduction	9.3
9.2	Income from Salaries—Chargeability	9.4
9.3	Income from Salaries—Basis of Charge	9.5
9.4	Format for Computing Taxable Salary	9.6
9.5	Provisions	9.7
9.6	Forms of Salary	9.7
9.6.1	Basic Salary	9.8
9.6.2	Advance Salary	9.10
9.6.3	Dearness Pay	9.10
9.6.4	Bonus	9.10
9.6.5	Commission	9.10
9.6.6	Fees	9.10
9.6.7	Interim Relief	9.10
9.6.8	Gratuity	9.10
9.6.9	Leave Salary or Salary in Lieu of Leave or Encashment of Earned Leave	9.21
9.6.10	Pension	9.30
9.7	Allowances Under Section 17(3)	9.37
9.8	Deductions Under Section 16	9.51
9.8.1	Entertainment Allowance under Section 16(ii)	9.51
9.8.2	Professional Tax or Employment Tax under Section 16(iii)	9.51
9.9	Provident Fund	9.52
9.10	Perquisites Under Section 17(2)	9.58
9.10.1	Tax Free Perquisites	9.59
9.10.2	Perquisites Taxable in the Hands of All Employees	9.66
9.10.3	Perquisites Taxable in the Hands of ‘Specified Employees’ Only	9.90

- 9.11 Profits in Lieu of or in Addition to Salary Under Section 17(3) 9.103
- Summary 9.123
- Theory Questions 9.125
- Exercises 9.127

Chapter 10 Income from House Property **10.1–10.74**

- 10.1 Chargeability 10.3
 - 10.1.1 Cases where Property Income is not Chargeable to Tax 10.6
- 10.2 Basis of Charge 10.6
- 10.3 Formats and Provisions 10.6
 - 10.3.1 Let-Out Property 10.6
 - 10.3.2 Self Occupied Property 10.25
 - 10.3.3 Deemed to be Let Out Property 10.29
 - 10.3.4 Partly Let Out and Partly Self-Occupied Property 10.34
- 10.4 Special Provisions Under the Head ‘Income From House Property’ 10.39
 - 10.4.1 Recovery of Unrealised Rent and Arrears of Rent Received [Section 25A] 10.40
 - 10.4.2 Property Owned by Co-owners [Section 26] 10.43
 - 10.4.3 House Property in a Foreign Country 10.47
- Summary 10.66
- Theory Questions 10.67
- Exercises 10.69

11. Income Tax Authorities **11.1–11.6**

- 11.1 Introduction 11.1
- 11.2 Central Board of Direct Taxes (CBDT) 11.2
- 11.3 Director General/Director 11.3
- 11.4 Commissioners of Income-tax 11.3
- 11.5 Commissioners (Appeals) 11.4
- 11.6 Joint Commissioners 11.4
- 11.7 Income-tax Officers 11.5
- 11.8 Inspectors of Income-tax 11.5
- Summary 11.5
- Theory Questions 11.6

Model Question Paper-1	M-1.1–M-1.4
Model Question Paper-2	M-2.1–M-2.4
Model Question Paper-3	M-3.1–M-3.4

Tax

CHAPTER OVERVIEW

- 1.1 Meaning of Tax
- 1.2 Characteristics of Tax
- 1.3 Classification of Tax
- 1.4 Income Tax
- 1.5 Importance of Income Tax
- 1.6 Brief History of Income Tax
- 1.7 Legal Framework of Income Tax in India
- 1.8 Canons of Taxation
- 1.9 Coverage or Scope of Income Tax Act, 1961
- 1.10 Steps in Assessment

MEANING OF TAX

1.1

Tax refers to compulsory contribution made by citizens of a country to the Government, for the benefits obtained from the Government.

According to Prof. Seligman “tax is a compulsory contribution from a person to the government to defray the expenses incurred in the common interest of all, without reference to special benefits conferred”.

CHARACTERISTICS OF TAX

1.2

The following are the characteristic features of Tax:

1. Tax is a **compulsory contribution** to be made by the citizens to the government.
2. The person paying tax **cannot expect any direct return** or benefit in proportion to the amount of tax paid by him.
3. Taxes are collected by the government for **providing common services** like education, health, electricity, water, roads, law and order, other infrastructure facilities and not for any specific service to the individual.

CLASSIFICATION OF TAX

1.3

The Government of any country levies various taxes on its citizens and all such taxes are broadly classified into two types, viz., **Direct Taxes** and **Indirect Taxes**.

1.2 • Income Tax-I

Direct Tax refers to the type of tax in which the incidence (i.e., liability for payment of tax) and impact (i.e., actual payment of tax) is on the same person. It is a form of tax which can be traced to the payer and it flows *directly* from the tax-payer to the Government.

Indirect Tax refers to the type of tax in which the incidence and impact are on different persons. It is a form of tax which cannot be traced to the payer and it flows from the payer to the Government *indirectly* – i.e., through others.

According to the Constitution of India, both direct and indirect taxes are levied in India by various authorities. The following table gives details of various authorities authorized to levy tax in India by the Indian Constitution and examples of such taxes levied:

Authority	Direct Taxes	Indirect Taxes
The Union Government	Income Tax (other than on Agricultural Income)	Excise Duty on Petroleum Products Customs Duty Central Goods and Services Tax Central Sales Tax
State Governments/ Union Territories	Tax on Agricultural Income, Professional or Employment Tax, etc.	Excise Duty on Liquor. State Goods and Services Tax/Union Territories Goods and Services Tax
Local Authority	Municipal Taxes on Property, Water Tax, etc.	Entry Tax etc.

This book provides a discussion on **Income Tax** – a Direct Tax levied by the Union Government.

INCOME TAX

1.4

Income Tax refers to tax on income. *Income* refers to return on investment, where the investment may be monetary or non-monetary. Similarly, return also could be monetary or non-monetary, real or notional, regular or casual, proportionate or dis-proportionate to investment.

In India, the levy, collection and monitoring of Income Tax is governed by the Income Tax Act of 1961. The Act has more than 400 sections, numerous sub-sections and fourteen schedules. It extends to the whole of India. An understanding of the system of levy and collection of income tax in India requires knowledge of provisions given in Income Tax Act, 1961 along with the Income Tax-Rules, 1962, Circulars and clarifications issued by the CBDT; and various judicial decisions.

IMPORTANCE OF INCOME TAX

1.5

The following points highlight the importance of Income Tax:

1. Income tax is an important source of income to the government.

2. It is used as an effective tool for reducing unequal distribution of income and wealth between rich and poor through different slabs of tax rates.
3. It is also used as a tool for reducing the regional economical imbalance through incentives and concessions in income tax to the industries set up in rural areas.

BRIEF HISTORY OF INCOME TAX

1.6

- Direct taxation existed in India in one form or the other from time immemorial. It dates back to the times of Ramayana and Mahabharatha.
- The famous *Manusmrithi* and *Arthashastra* contain various references to the taxes. Manu in his *Manusmrithi* has even suggested that tax should be levied not only upon income but also upon expenditure. He further says that tax policy should be framed by the Government in such a way that the citizens should never feel it as a burden and should never think of tax evasion and tax avoidance.
- During 300 B.C. the greatest economist and financial expert Kautilya explained beautifully the taxes and suggested that customs duty shall be charged on the persons who come from outside. He further stated that the power of Government is dependent upon the strength of its treasury.
- In 1860, Sir James Wilson, a British ruler introduced the present type of income tax in order to raise funds for meeting the financial losses suffered by the Government on account of “Sepoy Mutiny” which took place in the year 1857. It was first introduced as a temporary measure to take care of the financial difficulties at that time but later on it became a permanent feature with the passing of “The Indian Income Tax Act, 1886”. This Act remained in force till 1917 though several amendments were made to it from time to time.
- In 1918, this Act was replaced by a new Act called “Income Tax Act, 1918”. On the recommendation of the All India Tax Enquiry Committee, the Income Tax Act, 1918 was replaced by a new Act called “Income Tax Act, 1922”, which was in force till 1961.
- A number of amendments were incorporated into this Act from time to time which made the Income Tax Act, 1922 a very complicated, cumbersome and confusing Act.
- The Government of India, in the year 1956 constituted “Law Commission” to suggest measures to simplify the Income Tax Act and to prevent evasion of tax. In the meantime the Government also appointed the Direct Taxes Administration Committee to suggest various measures to minimize the inconveniences to the tax payers and to prevent evasion of tax.
- The Law Commission submitted its report in 1958 and the Direct Taxes Administration Committee submitted its report in 1959. On the recommendations of these two committees the Government of India replaced the Income Tax Act, 1922 with the present Income Tax Act, 1961 which came into force from 1st April, 1961.
- The Income Tax Act, 1961 applies to the **whole of India including Jammu and Kashmir**. This Act also has undergone several amendments from time to time.

LEGAL FRAMEWORK OF INCOME TAX IN INDIA

1.7

Income tax in India is governed and monitored by the following:

1. Income Tax Act, 1961 as amended from time to time.
2. The Finance Act, passed by the Parliament every year.
3. The Income Tax Rules, 1962 as framed and amended by the Central Board of Direct Taxes (CBDT) from time to time.
4. Judicial decisions.
5. The circulars, notifications, orders and executive instructions given by the CBDT from time to time.

1.7.1 The Finance Bill/Act

Generally in the month of February of each year, the Finance Minister of the Government of India presents a bill known as Finance Bill in the Parliament. In the bill, among others, the Finance Minister proposes:

- (a) amendments in direct and indirect taxes,
- (b) amendments in rates of direct and indirect taxes,
- (c) amendments in rates for deduction of tax at source, etc., in the Finance Bill.

When this bill is approved by both the houses of Parliament (i.e., Lok Sabha and Rajya Sabha) and assented by the President of India, it becomes Finance Act. Thereafter the provisions of Finance Act are incorporated in the Income Tax Act. The Finance Act also specifies the rates of tax for computation of income tax and other taxes.

CANONS OF TAXATION

1.8

Canons of taxation, also known as principles of taxation, refer to the guidelines laid down by various economists and statesmen for framing rules of taxation. Adam Smith, in his book “An inquiry into the nature and causes of the wealth of nations” laid down four Canons of taxation viz.,

- (1) Canon of ability,
- (2) Canon of economy,
- (3) Canon of convenience, and
- (4) Canon of certainty.

To these Canons of taxation, modern economists have added five more viz.,

- (1) Canon of productivity,
- (2) Canon of elasticity,
- (3) Canon of flexibility,
- (4) Canon of diversity, and
- (5) Canon of simplicity.

A brief explanation of these canons is given below:

1. *Canon of ability*: It states that the taxes imposed must be proportional to the ability of the citizens to pay. The taxpayers should not be made to pay tax beyond their capacity to pay. The tax should be based upon the principle of equity and justice. According to this principle a person with high income has higher capacity to pay tax and should be made to pay more tax; and a person with low income has less capacity to pay tax and should be made to pay less tax.
2. *Canon of economy*: It states that the cost of collecting tax must be less and economical.
3. *Canon of convenience*: It states that maximum convenience must be provided to the taxpayer to pay tax. For example, a salaried employee should be allowed to pay tax when he receives salary, a buyer should be allowed to pay tax when he buys the product and a farmer must be allowed to pay tax when he harvests the crop and so on.
4. *Canon of certainty*: It states that the payer of tax must have a certain idea about the mode, time, place and the amount of tax payable by him.
5. *Canon of productivity*: It states that the taxes imposed must be capable of producing more revenues and should not affect the production and distribution of the country.
6. *Canon of elasticity*: It states that rates of tax should be more elastic i.e., a slight reduction in tax rates should enable collection of more taxes.
7. *Canon of flexibility*: It states that tax policy should enable adjustments if needed.
8. *Canon of diversity*: It states that tax structure should be diversified i.e., there must be a diverse variety of taxes so that all categories of people are brought under the tax net.
9. *Canon of simplicity*: It states that the tax rules and procedures must be simple so that the tax payers are able to understand the details of taxes easily.

COVERAGE OR SCOPE OF INCOME TAX ACT, 1961

1.9

The Income Tax Act, 1961 covers mainly one component – ‘Assessment’. **Assessment** refers to the process of Computing Taxable Income, Calculating Tax on Taxable Income and imposing Tax Liability [Section 2(8)].

The entire discussion in the Act covers the following three areas:

1. Computation of taxable income of the **assessee** (assessee is the person who has earned income).
2. Calculating tax on such taxable income.
3. Procedures for making assessee pay the tax.

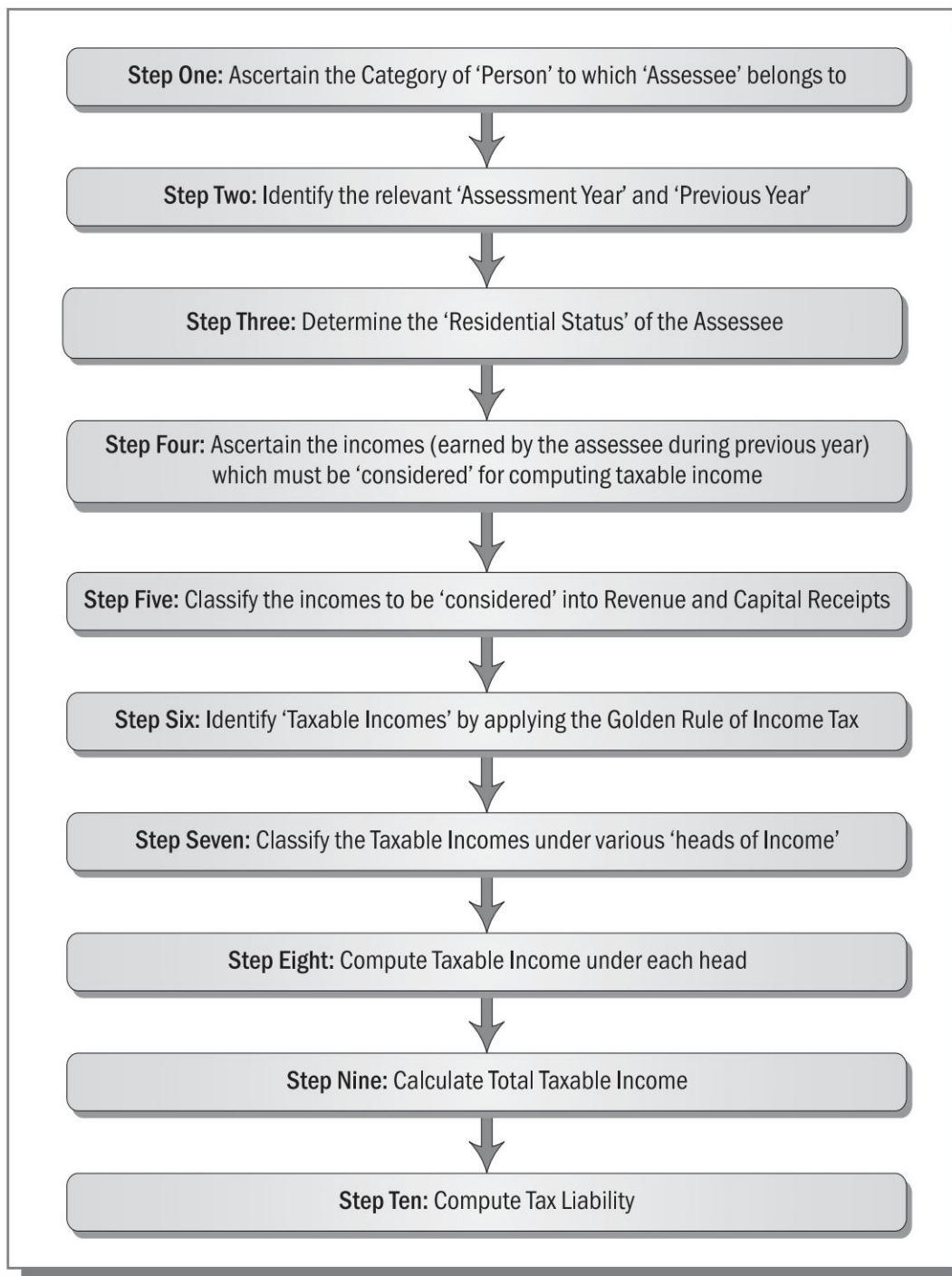
The process of these three stages is called ‘assessment’. Hence, the coverage of the Act is confined to one component – ‘Assessment’ and a detailed understanding of ‘how to make assessment?’ [i.e., how to compute taxable income, how to calculate tax liability and how to make assessee pay the tax] is the learning outcome expected from study of Income Tax Act and associated material.

This book provides a systematic approach for making ‘assessment’.

STEPS IN 'ASSESSMENT'

1.10

The following flow-chart provides an outline of the steps involved in making 'assessment':



A detailed discussion of each step in ‘making assessment’ is made in the following chapters.

SUMMARY

- **Tax** refers to compulsory contribution made by citizens of a country to the Government, for the benefits obtained from the Government.
- All taxes levied by any Government are of two types viz., Direct Taxes and Indirect Taxes.
- **Direct Tax** refers to the type of tax in which the incidence (i.e., liability for payment of tax) and impact (i.e., actual payment of tax) is on the same person. It is a form of tax which can be traced to the payer and it flows *directly* from the tax-payer to the Government.
- **Indirect Tax** refers to the type of tax in which the incidence and impact are on different persons. It is a form of tax which cannot be traced to the payer and it flows from the payer to the Government *indirectly* – i.e., through others.
- **Income Tax** is one of the forms of Direct Tax. It refers to tax on income. *Income* refers to return on investment, where the investment may be monetary or non-monetary.
- In India, the levy, collection and monitoring of Income Tax is governed by – Income Tax Act, 1961 as amended from time to time; the Finance Act, passed by the Parliament every year; the Income Tax Rules, 1962 as framed and amended by the Central Board of Direct Taxes (CBDT) from time to time; Judicial decisions; the circulars; notifications, orders; and executive instructions given by the CBDT from time to time.
- Various economists and finance experts have laid down principles for framing rules of taxation. Such principles are called Canons of taxation. The Canons which forms the foundation in designing tax laws are – Canon of ability, Canon of economy, Canon of convenience, Canon of certainty, Canon of productivity, Canon of elasticity, Canon of flexibility, Canon of diversity and Canon of simplicity.
- The Income Tax Act, 1961 covers mainly one component – ‘Assessment’. **Assessment** refers to the process of Computing Taxable Income, Calculating Tax on Taxable Income and Imposing Tax Liability.
- This chapter has highlighted the steps to be followed in making ‘assessment’.

THEORY QUESTIONS

Section A Type Questions

1. What is ‘Tax’?
2. State the different types of tax with their meanings.
3. Differentiate between ‘Direct Tax’ and ‘Indirect Tax’.
4. List the authorities empowered to levy taxes in India, according to the Constitution of India.
5. List the various direct and indirect taxes that can be levied by the Union Government.
6. Give examples of various taxes that can be levied by State Governments and Local Authorities.
7. What is Income Tax?
8. What is Income? List the features of income.
9. What is Finance Bill?
10. What is Finance Act?

1.8 • Income Tax-I

11. What is meant by 'canons of taxation'?
12. What is canon of ability?
13. What is canon of economy?
14. What is canon of convenience?
15. What is canon of certainty?
16. What is canon of productivity?
17. What is canon of elasticity?
18. What is canon of flexibility?
19. What is canon of diversity?
20. What is canon of simplicity?
21. What is 'Assessment'?

Section B Type Questions

1. Explain the different types of Tax and elaborate the taxonomy of taxation in India.
2. Briefly explain the importance of tax.
3. Briefly explain the history of income tax.
4. What is meant by canons of taxation? Briefly explain the various canons of taxation.
5. List out the steps in making 'Assessment'.

STEP ONE: ASCERTAIN THE CATEGORY OF 'PERSON' TO WHICH 'ASSESSEE' BELONGS TO



Step Two: Identify the relevant 'Assessment Year' and 'Previous Year'



Step Three: Determine the 'Residential Status' of the Assessee



Step Four: Ascertain the incomes (earned by the assessee during previous year) which must be 'considered' for computing taxable income



Step Five: Classify the incomes to be 'considered' into Revenue and Capital Receipts



Step Six: Identify 'Taxable Incomes' by applying the Golden Rule of Income Tax



Step Seven: Classify the Taxable Incomes under various 'heads of Income'



Step Eight: Compute Taxable Income under each head



Step Nine: Calculate Total Taxable Income



Step Ten: Compute Tax Liability

2

Assessee and Person

CHAPTER OVERVIEW

2.1 Assessee

2.2 Person

- The FIRST STEP in making assessment is
- ascertaining the category of 'person' to which
- 'assessee' belongs to.

ASSESSEE [SECTION 2(7)]

2.1

'Assessee' means a person by whom any tax or any other sum of money is payable under this Act and includes the following:

- (i) Every person in respect of whom any proceeding under the Income Tax Act has been taken:
 - (a) for the assessment of his income or the income of any other person in respect of which he is assessable; or
 - (b) to determine the loss sustained by him or by such other person; or
 - (c) to determine the amount of refund due to him or to such other person.
- (ii) Every person who is deemed to be an assessee under any provision of this Act; and
- (iii) Every person who is deemed to be an assessee in default under any provisions of this Act.

Notes:

- (a) 'Any tax' in the above definition includes income tax, surcharge, Education Cess and Secondary and Higher Education Cess.
- (b) 'Any other sum of money' in the above definition includes fees, interest, fines, penalty, etc.
- (c) 'Deemed to be an assessee' means that the assessee is treated as an assessee, although he is not assessable for his income or loss or refund. This category includes legal representatives, representatives of deceased persons, guardians of minor children, etc.

- (d) A person is said to be ‘assessee in default’ if he fails to comply with the duties imposed upon him under the Income Tax Act. For example, an assessee who was liable to deduct tax at source from the payment to be made, but either does not deduct or deducts but does not remit to the Department, is an assessee in default.

PERSON [SECTION 2(31)]

2.2

‘Person’ includes—

- (i) An Individual,
- (ii) A Hindu Undivided Family,
- (iii) A Company,
- (iv) A Firm,
- (v) An Association of Persons or a Body of Individuals, whether incorporated or not,
- (vi) A Local Authority,
- (vii) Every Artificial Juridical person not falling within any of the preceding sub-clauses.

Notes:

- (a) ‘An Individual’ means a natural person.
- (b) As per the Hindu Law, ‘Hindu Undivided Family’ means a family which consists of all persons lineally descended from a common ancestor including their wives and daughters.
- (c) ‘Company’ means—
 - (i) Any Indian company; or
 - (ii) Any “Body Corporate” incorporated under the laws of a foreign country; or
 - (iii) Any institution, association or a body which is assessed or was assessable/assessed as a company for any assessment year commencing on or before April 1, 1970; or
 - (iv) Any institution, association or a body, whether incorporated or not and whether Indian or non-Indian, which is declared by general or special order of the Central Board of Direct Taxes to be a company.
- (d) Section 4 of the Indian Partnership Act, 1932, defines partnership as “relationship between persons who have agreed to share the profits of business carried on by all or any of them acting for all”. Persons who have entered into partnership with one another are individually called partners and collectively a **firm** and the name under which the business is carried on is called the **firm name**.
- (e) ‘Association of Persons’ means *two or more persons* who join a common purpose with a view to earn an income, but do not constitute a partnership.
- (f) ‘Body of Individuals’ means a conglomeration of individuals who carry on some activity with the objective of earning some income. It consists only individuals and any other

category of persons (i.e., companies, firms etc.) cannot be members of a body of individuals.

- (g) 'Association of Persons' and 'Body of Individuals' include Societies, Clubs, Trusts, Unions, etc.
- (h) 'Local Authority' means–
 - (i) Panchayat; or
 - (ii) Municipality; or
 - (iii) Municipal Committee and District Board, legally entitled to, or entrusted by the Government with the control or management of a Municipal or local funds; or
 - (iv) Cantonment Board.
- (i) 'Artificial Juridical Person' is an entity which has a separate recognition for legal purposes. It includes Gods, Idols and Deities; and Statutory Corporations (i.e., Entities established with enactment of legislation either at Parliament or at Legislative Assembly).
- (j) An association of persons or a body of individuals or a local authority or an artificial juridical person shall be deemed to be a person, whether or not, such person or body or authority or juridical person, was formed or established or incorporated with the object of deriving income, profits or gains.

When an assessee (a shorter meaning for our requirement is – a person who has earned income) approaches us, seeking help in making his 'assessment' – the first step is to ascertain the category of 'person' to which the assessee belongs to.

Illustration 1 Problem on Ascertaining the category of 'Person' of the Assessee

Ascertain the category of 'person' of the following assesseees:

1. Mr. Ram
2. Lord Rama
3. Ram Seva Trust
4. Ram & Sons Ltd.
5. Ram & Brothers
6. Ram & Co.
7. Bharatiya Samskriti Vidyapeeth College for Women
8. Life Insurance Corporation of India
9. Bangalore University
10. Ayub Khan and Family
11. BHEL Employees Union
12. Institute of Chartered Accountants of India
13. Bruhat Bengaluru Mahanagara Palike

2.6 • Income Tax - I

Solution:

Assessee	Category of 'Person'
Mr. Ram	Individual
Lord Rama	Artificial Juridical Person
Ram Seva Trust	Body of Individuals or Association of Persons
Ram & Sons Ltd.	Joint Stock Company (It is mandatory for Companies to use 'Limited' or 'Private Limited' in the name).
Ram & Brothers	Hindu Undivided Family (Where the entity is governed by a Partnership Deed – it can also be considered as a ' Firm ')
Ram & Co.	Firm (if governed by a Partnership Deed) Body of Individuals (when not governed by a Partnership Deed, and consists of only Individuals) Association of Persons (when not governed by a Partnership Deed, and consists of different categories of persons)
Bharatiya Samskriti Vidyapeeth College for Women	Body of Individuals or Association of Persons (since in India, educational institutions are managed by a 'Trust' and 'Trusts' fall under BOI/AOP). Company (where the educational institution is managed by a Company – Public or Private) Note: The 'Trust' or the 'Company' managing the education institution is the assessee and not the institution per se.
Life Insurance Corporation of India	Artificial Juridical Person
Bangalore University	Artificial Juridical Person
Ayub Khan and Family	Firm (if governed by a Partnership Deed) Body of Individuals (when not governed by a Partnership Deed, and consists of only Individuals) Association of Persons (when not governed by a Partnership Deed, and consists of different categories of persons) Note: It is not a Hindu Undivided Family.
BHEL Employees Union	Body of Individuals
Institute of Chartered Accountants of India	Artificial Juridical Person
Bruhat Bengaluru Mahanagara Palike	Local Authority

SUMMARY

- In making assessment – the first step is to identify the category of ‘person’ to which ‘assessee’ belongs to.
- ‘Assessee’ refers to a ‘person’ who owes any sum of money to the Income Tax Department, to whom the department owes any sum of money, on which income tax proceedings have been carried out. ‘Assessee’ includes ‘deemed assessees’ and ‘assessees in default’.
- ‘Person’ includes individuals, Hindu undivided families, companies, firms, body of individuals or association of persons, local authorities and every other artificial juridical person.

THEORY QUESTIONS

Section A Type Questions

1. Define ‘Assessee’ in accordance with the Income Tax Act, 1961.
2. Who is a ‘deemed assessee’? Give examples.
3. Who is an ‘assessee in default’? Give examples.
4. Who is a ‘person’?
5. What is a ‘Hindu Undivided Family’?
6. What is a ‘Firm’?
7. Define ‘Company’ according to the Income Tax Act, 1961.
8. What is an ‘Association of Persons’?
9. What is a ‘Body of Individuals’?
10. What is a ‘Local Authority’?
11. What does ‘Artificial Juridical Persons’ include?

Section B Type Questions

1. Who is an ‘Assessee’? Explain with suitable examples.
2. Define ‘Person’ according to Income Tax Act, 1961 and explain the meaning and inclusion of each category, with examples.

EXERCISES

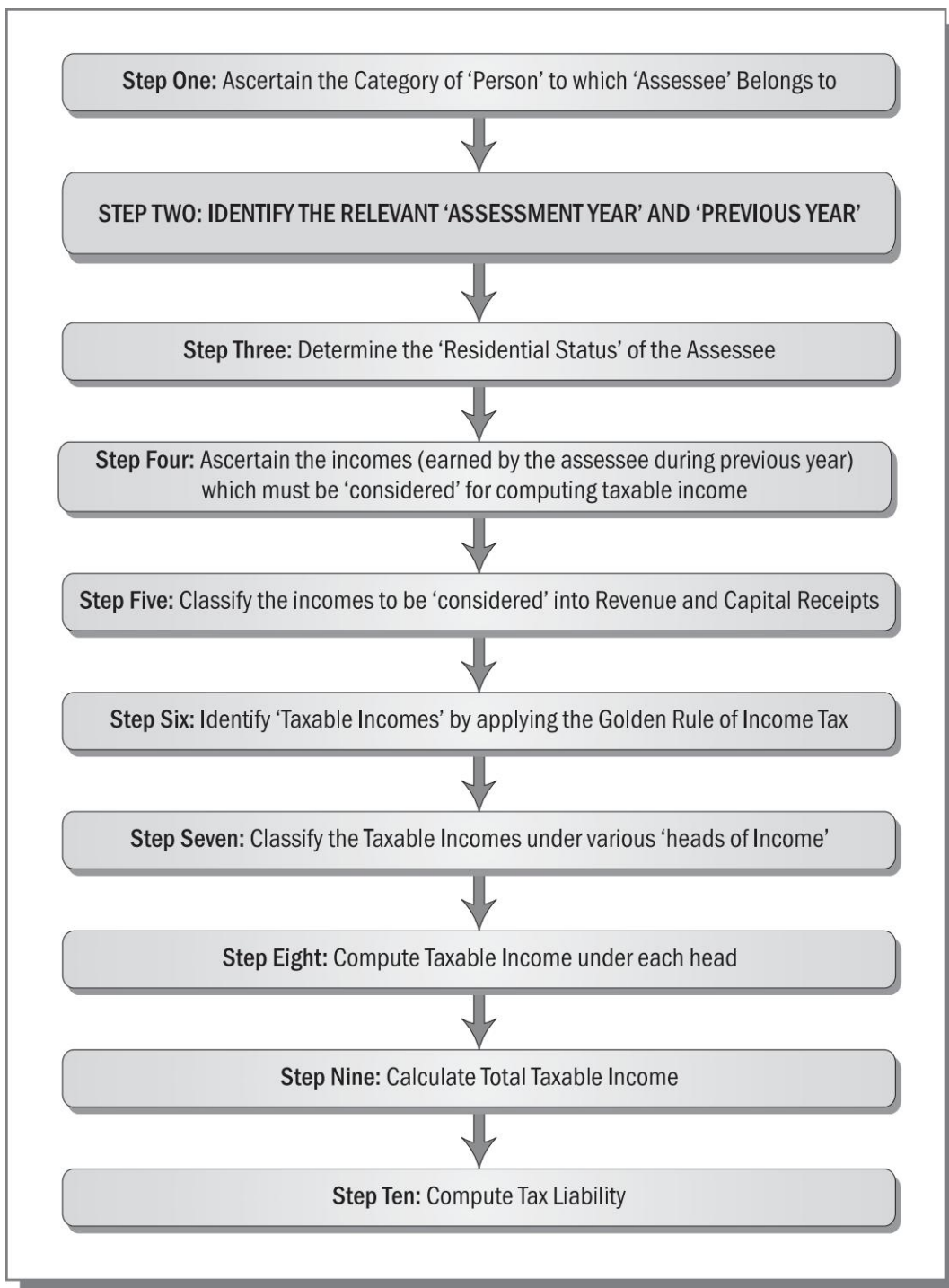
Ascertain the category of ‘person’ of the following assesseees:

1. Ms. Shashikala
2. Kandala Brothers LLP
3. BHS Higher Education Society
4. Center for Economic and Social Studies
5. Bangalore Central University
6. McGraw-Hill Education (India) Pvt. Ltd.
7. Holla-Mitran & Co.

2.8 • Income Tax-I

8. Suraj and Family
9. BMRCL Employees Union
10. Delhi Development Authority

(Ans: (1) Individual (2) Firm (3) BOI/AOP (4) Artificial Juridical Person (5) Artificial Juridical Person (6) Company (7) Firm (8) Hindu Undivided Family (9) BOI/AOP and (10) Local Authority)



3

Assessment Year and Previous Year

CHAPTER OVERVIEW

- 3.1 Assessment Year
- 3.2 Previous Year
- 3.3 General Rule of Previous Year and Exceptions to the Rule

The SECOND STEP in making assessment is to identify the year in which income earned by the assessee must be assessed – i.e., Assessment Year. Since the provisions for making assessment undergo changes each year, the assessee must be assessed according to the provisions applicable to the relevant year of earning income.

3.1

ASSESSMENT YEAR [SECTION 2(9)]

‘Assessment year’ refers to the period of twelve months commencing from the 1st April of each year, and ending on the 31st March of the following year. It is the period during which ‘assessment’ of assessee’s income of *previous year* will be made.

That is, assessment year is the period during which computation of taxable income of the assessee for his income earned during previous year, calculation of tax liability on such taxable income and imposing of tax liability on the assessee happens. At present, the Assessment Year is **2018-19 (i.e., 1st April, 2018 to 31st March, 2019)**

3.2

PREVIOUS YEAR [SECTION 3]

‘Previous Year’ refers to the financial year immediately preceding the assessment year. It is a period of twelve months which immediately precedes the assessment year. It is the year in which assessee earns income. For assessment year 2018-19, the relevant previous year is **2017-18 (i.e., 1st April, 2017 to 31st March, 2018).**

Notes:

1. In case of a business or profession which has been newly set up, or a source of income newly coming into existence in the said financial year, the previous year shall be the

period beginning from the date on which the new business or profession is set up or new source of income comes into existence, and ending on the last day of the financial year (i.e., 31st March). For example, if assessee sets up a new business and commences it from 2nd January, 2018, then the previous year will be from 2nd January, 2018 to 31st March, 2018.

2. The terms 'Assessment Year' and 'Previous Year' are to be used together and have no relevance independently.

GENERAL RULE OF PREVIOUS YEAR AND EXCEPTIONS TO THE RULE

3.3

According to the Income Tax Act, 1961, income earned by an assessee in any financial year is assessed in the immediately following financial year. This is regarded as the '*general rule of previous year*'. The financial year in which assessee earns income is called 'previous year' and the immediately following financial year in which such income is assessed is called 'assessment year'.

However, in the following situations or circumstances, income earned by the assessee must be assessed in the financial year of earning the income, and not in the immediately following financial year. Such situations are called '*Exceptions to the General Rule of Previous Year*'. The following are the exceptions:

1. **Income of Non-residents from Shipping Business [Section 172]**

Where the assessee is a non-resident who is carrying on a shipping business and earns income from carrying passengers or livestock or goods from a port in India, such income must be assessed before the ship is allowed to leave the Indian port. That is, income in this case must be assessed in the year of earning the income, and not in the following financial year.

2. **Income of persons leaving India [Section 174]**

Where the assessee is intending to leave India with no present intention of returning to India, the income earned by such assessee (actual or estimated) till the probable date of departure must be assessed before the assessee leaves India.

3. **Income of an association of persons or body of individuals or artificial juridical person formed for a particular event or purpose [Section 174A]**

Where the assessee being an association of persons or body of individuals or an artificial juridical person formed for a particular event or purpose, is likely to dissolve the entity during the same financial year in which it was formed or established or incorporated, the income of such person or body or juridical person till the date of likely dissolution must be assessed in the year of dissolution.

4. **Income of a person likely to transfer property to avoid tax [Section 175]**

Where the assessee is likely to charge, sell, transfer or dispose of any of his assets with a view to avoid payment of his tax liability, the income from such asset till the date of likely transfer must be assessed in the year of transfer.

5. Income of a discontinued Business [Section 176]

Where any business or profession is discontinued by the assessee during the financial year, the income from such business or profession for the financial year till the date of discontinuation can be assessed by the assessing officer in the year of discontinuance. However, the assessing officer can make the assessment in the following financial year, if he so desires, in this case.

In this book, the provisions explained and problems solved are as per law applicable for **Assessment Year 2018 -19** (i.e., for Previous Year **2017-18**).

Illustration 1 Problem on identification of Assessment Year and Previous Year

State the Previous Year and Assessment Year for the following:

1. Salary earned for the month of January, 2018.
2. Rent received for the month of February, 2018.
3. Professional income earned between 1st November, 2016 & 15th March, 2017 by a person leaving India.
4. Profit on sale of residential site on 1st January, 2017 by a person likely to transfer property to avoid tax.
5. Business income earned during 1st January, 2017 & 25th March, 2017 by a discontinued business.

Solution:

Sl. No.	Transaction	Relevant Previous Year and Assessment Year	Remarks
1.	Salary earned for the month of January, 2018	PY 2017-18 AY 2018-19	Since, the income is earned during financial year 2017-18, the relevant previous year is 2017-18 and assessment year is 2018-19.
2.	Rent received for the month of February, 2017	PY 2017-18 AY 2018-19	Since, the income is earned during financial year 2017-18, the relevant previous year is 2017-18 and assessment year is 2018-19.
3.	Professional income earned between 1 st November, 2016 & 15 th March, 2017 by a person leaving India	PY 2016-17 AY 2016-17	This is a case of exception to the 'General Rule of Previous Year' covered under section 174 (i.e., income of a person leaving India). Hence, both Previous year and Assessment Year is same (i.e., 2016-17).
4.	Profit on sale of residential site on 1 st January, 2017 by a person likely to transfer property to avoid tax	PY 2016-17 AY 2016-17	This is a case of exception to the 'General Rule of Previous Year' covered under section 175 (i.e., income of a person likely to transfer property for avoiding tax). Hence, both Previous year and Assessment Year is same (i.e., 2016-17).

3.6 • Income Tax-I

Sl. No.	Transaction	Relevant Previous Year and Assessment Year	Remarks
5.	Business income earned during 1 st April, 2017 & 25 th December, 2017 by a discontinued business	PY 2017-18 AY 2017-18	This is a case of exception to the 'General Rule of Previous Year' covered under section 176 (i.e., income of a discontinued business). Hence, both Previous Year and Assessment Year is same (i.e., 2017-18).

SUMMARY

- The second step in making assessment is ascertaining the year in which assessment has to be made.
- Since the provisions for assessment undergo change each year, the assessment cannot be accurate, unless the year of assessment is identified.
- Assessment year is the year in which assessee's income of the previous year is assessed. That is, it is the year in which computation of taxable income and tax liability of assessee's previous year income is carried out.
- Assessment year is a period of 12 months commencing from 1st April of each year and ending on 31st March of the following year.
- The present assessment year is 2018-19 (i.e., 1st April 2018 till 31st March 2019).
- Previous Year is a period of 12 months immediately preceding the assessment year. It is the period, the income earned during which, is assessed in the assessment year.
- For assessment year 2018-19, the relevant previous year is 2017-18 (i.e., 1st April 2017 till 31st March 2018).
- Usually, income earned in one financial year is assessed in the following financial year. This is called the 'general rule of previous year'. However, in few cases, the income is assessed in the year in which it is earned. Such cases are called exceptions to the general rule of previous year.
- The exceptions to the 'general rule of previous year' are – Income of non-residents from shipping business, income of persons leaving India, Income of a Body of Individuals or Association of Persons or an Artificial Juridical Person formed for a particular purpose, Income of a person who is likely to transfer assets for avoiding tax, and income of a discontinued business.

THEORY QUESTIONS

Section A Type Questions

1. What is 'Assessment Year'?
2. What is 'Previous Year'?
3. What is the Previous Year for a business or profession newly set up or for a new source of income?
4. What is 'General Rule of Previous Year'?
5. List the exceptions for the 'General Rule of Previous Year'.

Section B Type Questions

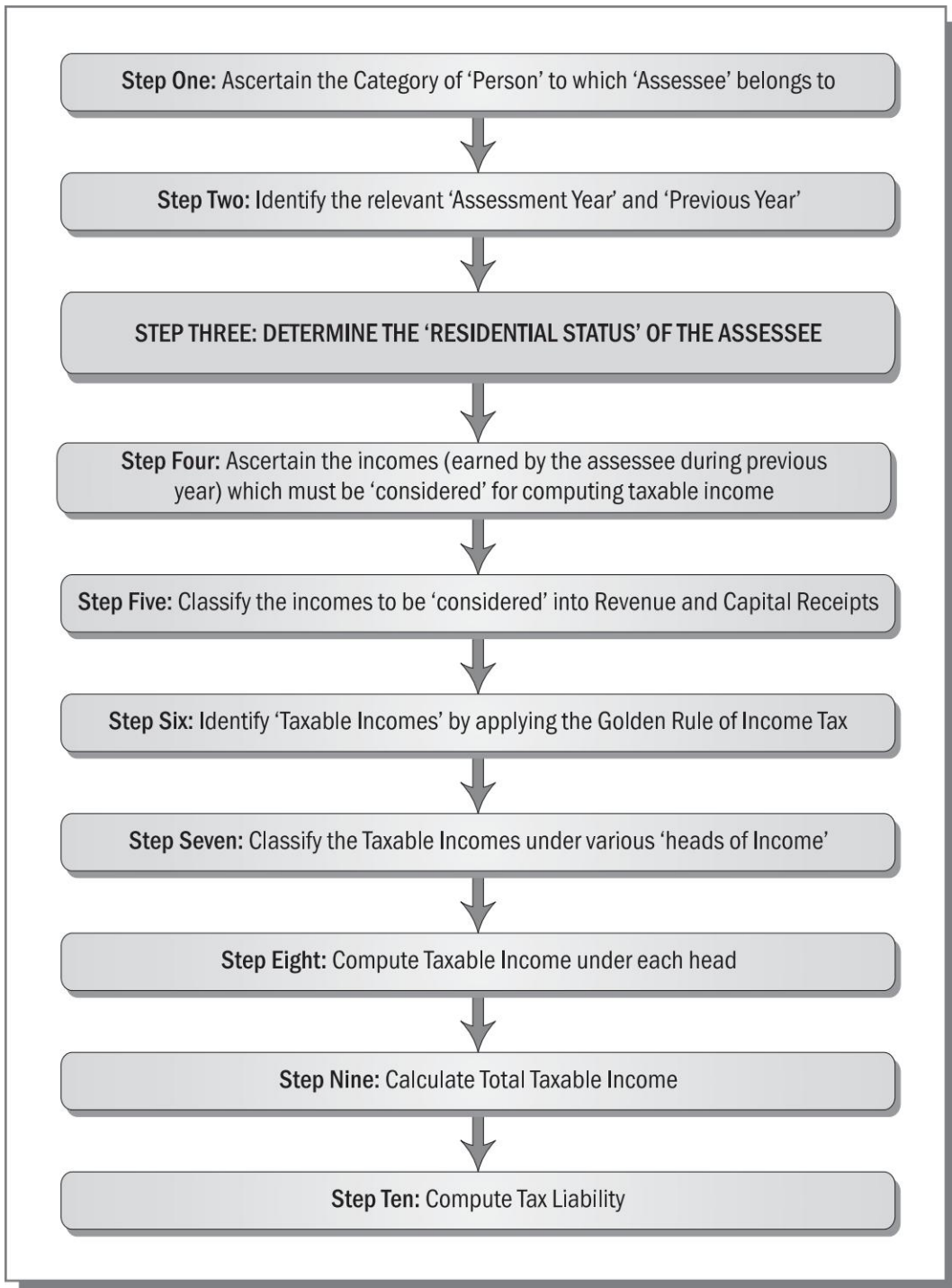
1. What is 'Previous Year'? Explain the concept of 'General Rule of Previous Year' and the exceptions to the Rule.

EXERCISES

1. What is the Assessment Year and Previous Year for the salary received on 1st January, 2018.
2. What is the Assessment Year and Previous Year for the income earned on 1st January, 2017 by a non-resident from a shipping business?
3. What is the Assessment Year and Previous Year for the rental income earned from house property on 1st January, 2018?
4. What is the Assessment Year and Previous Year for the professional income earned from 1st April 2017 to 31st January, 2018 by a person leaving India permanently?
5. What is the Assessment Year and Previous Year for the profit on sale of residential house earned on 1st January, 2017 by a person likely to transfer property to avoid tax?
6. What is the Assessment Year and Previous Year for the interest on fixed deposits earned for the period from 1st November, 2017 to 28th February, 2018?
7. What is the Assessment Year and Previous Year for the income earned from 1st July, 2016 to 31st January, 2017 by a discontinued business?

(Ans)

Sl. No.	Previous Year	Assessment Year
1	2017-18	2018-19
2	2016-17	2016-17
3	2017-18	2018-19
4	2017-18	2017-18
5	2016-17	2016-17
6	2017-18	2018-19
7	2016-17	2016-17



4

Residential Status

CHAPTER OVERVIEW

- 4.1 Meaning and Introduction
- 4.2 Residential Status of Individual Assessee

In assessing the income of the assessee, after ascertaining the category of 'person' to which assessee belongs to, and the assessment year applicable to him, the **next step** is to determine 'residential status' of the assessee for the relevant previous year.

In this chapter, determination of 'residential status' for Individual assessee for Previous Year 2017-18 (as applicable to Assessment Year 2018-19) has been discussed.

MEANING AND INTRODUCTION

4.1

'Residential Status' refers to status of the assessee based on residence (i.e., stay) in India. For the purpose of determining residential status, assessee is classified into the following categories:

1. Individuals,
2. Hindu Undivided Families,
3. Companies,
4. Firms,
5. Other Assessee (which includes Association of Persons or Body of Individuals, Local Authority and Artificial Juridical Person)

RESIDENTIAL STATUS OF INDIVIDUAL ASSESSEES

4.2

The residential Status of an Individual is basically classified into two categories, viz.,

- A. Resident
- B. Non-resident

4.4 • Income Tax -I

An individual is said to be a 'resident' if he fulfills **at least** one of the two conditions given under section 6(1).

An individual is said to be a 'non-resident', if he fulfills none of the conditions given under section 6(1).

When an individual becomes a 'resident' by virtue of fulfilling at least one condition under section 6(1), his status is further classified into two categories, viz.,

- A. Resident and ordinarily a resident.
- B. Resident but not ordinarily a resident.

A resident individual, who fulfills both of the two conditions given under section 6(6) is a 'resident and ordinarily a resident'.

A resident individual, who fulfills one or none of the two conditions given under section 6(6) is a 'resident, but not ordinarily a resident'.

On the whole, the residential status of an individual is classified into three categories, viz.,

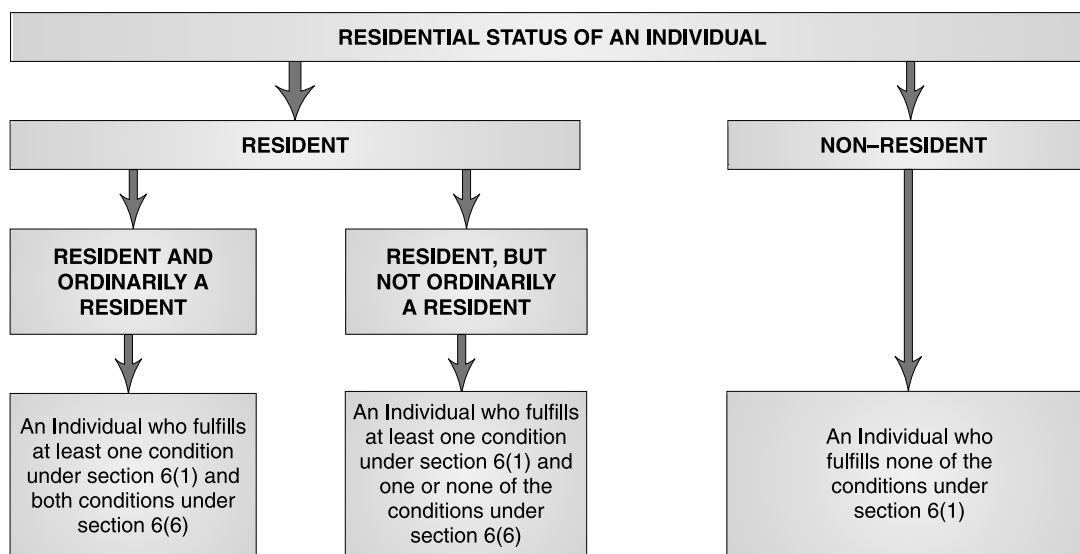
- 1. Resident and ordinarily a resident
- 2. Resident but not ordinarily a resident
- 3. Non-resident

An individual who fulfills at least one condition under section 6(1) **and** both conditions under section 6(6) is '**resident and ordinarily a resident**'.

An individual who fulfills at least one condition under section 6(1) **and** one or none of the conditions under section 6(6) is '**resident, but not ordinarily a resident**'.

An individual who fulfills none of the conditions under section 6(1) is a '**non-resident**'.

The following is the diagrammatic representation of the provisions for determining residential status of an Individual assessee:



Conditions under Section 6(1)

(a) The individual must be in India for at least 182 days during the relevant previous year.

OR

(b) The individual must be in India for at least 60 days during the relevant previous year,

and

at least 365 days during four previous years immediately preceding the relevant previous year.

Notes:

1. 'Being in India' can be 'anywhere in India' including territorial waters of India.
2. The Number of days of stay specified in the condition need not be continuous stay.
3. For counting the number of days of stay in India, both the ***date of arrival*** into India and ***date of departure*** from India, must be considered.
4. In the following cases, 60 days in condition under section 6(1)(b) must be replaced by 182 days (i.e., in the following cases, the second condition is the same as first condition):
 - (a) In case of an Indian citizen leaving India for employment purposes;
 - (b) In case of an Indian citizen leaving India as a crew member of a ship;
 - (c) In case of a person of Indian Origin coming on a visit to India or for permanent stay in India.
5. In case of an **Indian citizen leaving India as a crew member of a foreign bound ship**, the period of stay of the individual in India shall ***not include*** – the period commencing from the date entered into the *Continuous Discharge Certificate* in respect of **joining the ship** for the eligible voyage and ending on the date entered into the *Continuous Discharge Certificate* in respect of **signing off by that individual from the ship** in respect of such voyage. ('**Eligible Voyage**' for this purpose means a voyage undertaken by a ship engaged in the carriage of passengers or freight in international traffic which has originated from any port in India and has its destination of any port outside India, or a voyage which has originated from any port outside India and has destination of any port in India).
6. For becoming resident, an individual need to fulfill at least one of the conditions under section 6(1). In the above mentioned three cases, where an individual fulfills the first condition, he doesn't have to verify the fulfillment of the second condition; and where he cannot fulfill the first condition, the second condition also cannot be fulfilled. So, in the above three cases, the second condition [i.e., condition under section 6(1)(b)] is not required at all). Hence, the above three cases are called 'Exceptions to condition under section 6(1)(b)'.
 7. 'Person of Indian Origin' means an individual whose either of the parents, or any of the grand-parents were born in undivided India.

4.6 • Income Tax-I

Conditions Under Section 6(6)

- (i) The Individual must be **resident in India** for at least two out of ten previous years immediately preceding the relevant previous year,

AND

- (ii) The Individual must be in India for at least 730 days during seven previous years immediately preceding the relevant previous year.

Note: Section 6(6)(i) is fulfilled when the individual fulfills at least one condition u/s 6(1) for at least two out of ten previous years immediately preceding the previous year.

PROBLEMS ON DETERMINATION OF RESIDENTIAL STATUS

Illustration 1 Problem on determination of Residential Status of Individuals

Mr. Nicholas is a citizen of Slovenia. The details of his arrival in India and departure from India are as under:

ARRIVAL	DEPARTURE
02-02-2008 (first time)	30-06-2008
01-06-2010	28-06-2010
01-08-2010	28-02-2011
20-12-2011	31-01-2013
02-02-2014	01-06-2014
01-05-2015	29-10-2015
01-01-2017	04-03-2017
01-10-2017	30-11-2017

Determine his residential status for the assessment year 2018-19.

Solution:

Step 1: Calculation of Number of Days of Stay in India during different previous years

[illegible]

P.Y	APR	MAY	JUN	JUL	AUG	SEP	OCT	NOV	DEC	JAN	FEB	MAR	TOT
2008-2009	30	31	30	0	0	0	0	0	0	0	0	0	91
2007-2008	0	0	0	0	0	0	0	0	0	0	29	31	60

Notes:

1. While counting the number of days of stay, both date arrival and date of departure has been considered.
2. In the month of June 2010, Mr. X arrives on 1st and departs on 28th. Including the dates of arrival and departure, the total number of days of stay during June 2010 is 28.

Step 2: Verification of Fulfillment of Conditions Under Section 6(1)

Condition Under Section 6(1)	Fulfilled or Not Fulfilled
(a) The Individual must be in India for at least 182 days during the relevant previous year (i.e., 2017-18)	Not Fulfilled
(b) The Individual must be in India for at least 60 days during the relevant previous year (i.e., 2017-18)	Fulfilled
and at least 365 days during four previous years immediately preceding the relevant previous year (i.e., between 01.04.2013 and 31.03.2017)	Fulfilled

Since Nicholas has fulfilled one of the conditions under section 6(1), he is a **resident**.

Notes:

1. Since Mr. X is a foreign citizen 60 days has been taken in the condition under section 6(1)(b). Where the assessee was either an Indian citizen leaving India for employment purposes or an Indian citizen leaving India as a crew member of a ship or a Person of Indian Origin coming to India, 182 days must have been taken in the same condition.
2. The total number of days of stay during 4 previous years immediately preceding the relevant previous year (i.e., between 01.04.2013 and 31.03.2017) is **365** (63 + 182 + 62 + 58).
3. Condition under section 6(1)(b) is said to be fulfilled if both the parts of the condition are fulfilled.

Step 3: Verification of Fulfillment of Conditions under Section 6(6)

Condition Under Section 6(6)	Fulfilled or Not Fulfilled
(i) The Individual must be a resident in India for at least 2 out of 10 previous years immediately preceding the relevant previous year (i.e., 2017-18)	Fulfilled
(ii) The Individual must be in India for at least 730 days during 7 previous years immediately preceding the relevant previous year (i.e., between 01.04.2010 and 31.03.2017)	Fulfilled

Since Mr. Nicholas, a resident individual, has fulfilled both the conditions under section 6(6), he is a **‘resident and ordinarily a resident’**.

Notes:

1. Condition under section 6(6)(i) requires the individual to be **‘resident’** for at least two out of 10 previous years immediately preceding the previous year. Being ‘resident’ means fulfilling at least one of the conditions under section 6(1). In this case, Mr. X is resident for previous years 2010-11, 2011-12, 2012-13, 2014-15, 2015-16 and 2016-17 by fulfilling either of the two conditions under section 6(1). That is, out of 10 previous years immediately preceding the relevant previous year, X is resident for 6 years. Hence, the first condition is fulfilled.
2. The number of days of stay during 7 previous years immediately preceding the relevant previous year (i.e., 2017-18) is **1014** (63 + 182 + 62 + 58 + 306 + 103 + 240). Hence, the condition under section 6(6)(ii) is fulfilled.

Illustration 2 Problem on Determination of Residential Status of Individuals

In the above problem, what will be the residential status of Mr. Nicholas, if he departs on 3rd March 2017, instead of 4th March, 2017.

Solution:

In this case, the number of days of stay of Mr. Nicholas in India, during previous year 2016-17 will be 62 days (since during March 2017, his stay will be only 3 days). On account of this, the total number of days of stay during 4 previous years immediately preceding the relevant previous year will be **364** (62 + 182 + 62 + 58).

Mr. Nicholas neither fulfills condition under section 6(1)(a) nor the condition under section 6(1)(b). Hence, he becomes a ‘**Non-resident**’. Since, Mr. Nicholas is a non-resident, there is no need to verify the fulfillment of conditions under section 6(6).

Illustration 3 Problem on Determination of Residential Status of Individuals

Mr. Ram an Indian citizen left India on 22.09.2017 for the first time to work as an officer of a company in Germany. Determine the residential status of Ram for the assessment year 2018-19 and explain the conditions to be fulfilled for the same under the Income Tax Act, 1961.

Solution:

Step 1: Calculation of Number of Days of Stay in India during different previous years

[illegible]

P.Y	APR	MAY	JUN	JUL	AUG	SEP	OCT	NOV	DEC	JAN	FEB	MAR	TOT
2011-2012													366
2010-2011													365
2009-2010													365
2008-2009													365
2007-2008													366

Step 2: Verification of Fulfillment of Conditions Under Section 6(1)

Condition Under Section 6(1)	Fulfilled or Not Fulfilled
(a) The Individual must be in India for at least 182 days during the relevant previous year (i.e., 2017-18)	Not Fulfilled
(b) The Individual must be in India for at least 182 (see note 1) days during the relevant previous year (i.e., 2017-18) and at least 365 days during four previous years immediately preceding the relevant previous year (i.e., between 01.04.2013 and 31.03.2017)	Not Fulfilled Fulfilled

Since Ram has not fulfilled any of the conditions under section 6(1), he is a **non-resident**.

Notes:

1. Ram is an Indian citizen leaving India for employment purposes. This is a case of exception to condition under section 6(1)(b). Hence, in the condition 60 days has been replaced by 182 days.
2. Alternatively, fulfillment of condition under section 6(1)(a) only can be verified. In case it is fulfilled, assessee becomes a resident. Else, he would be a non-resident.

Illustration 4 Problem on Determination of Residential Status of Individuals

Bret Lee, an Australian cricket player visits India for 100 days in every financial year. This has been his practice for the past 10 financial years. Find out his residential status for the assessment year 2018-19.

(Bangalore University, B.Com, December 2015)

Solution:

Step 1: Calculation of Number of Days of Stay in India during different previous years

PREVIOUS YEAR	TOTAL
2017-2018	100
2016-2017	100
2015-2016	100
2014-2015	100

4.10 • Income Tax-I

PREVIOUS YEAR	TOTAL
2013-2014	100
2012-2013	100
2011-2012	100
2010-2011	100
2009-2010	100
2008-2009	100
2007-2008	100

Step 2: Verification of Fulfillment of Conditions Under Section 6(1)

Condition Under Section 6(1)	Fulfilled or Not Fulfilled
(a) The Individual must be in India for at least 182 days during the relevant previous year (i.e., 2017-18)	Not Fulfilled
(b) The Individual must be in India for at least 60 days during the relevant previous year (i.e., 2017-18)	Fulfilled
and at least 365 days during four previous years immediately preceding the relevant previous year (i.e., between 01.04.2013 and 31.03.2017)	Fulfilled

Since Bret Lee has fulfilled both the conditions under section 6(1), he is a **resident in India** for assessment year 2018-19.

Note:

Bret Lee is a foreign citizen. Hence, for verification of fulfillment of condition under section 6(1)(b), 60 days have been considered.

Step 3: Verification of Fulfillment of Conditions Under Section 6(6)

Condition Under Section 6(6)	Fulfilled or Not Fulfilled
(i) The Individual must be resident in India for at least 2 out of 10 previous years immediately preceding the relevant previous year (i.e., 2017-18)	Fulfilled
(ii) The Individual must be in India for at least 730 days during 7 previous years immediately preceding the relevant previous year (i.e., between 01.04.2010 and 31.03.2017)	Not Fulfilled

Since Bret Lee, a resident individual, has fulfilled only one of the conditions under section 6(6), he is a **‘resident, but not ordinarily a resident’**.

Notes:

1. For every previous year, preceding the relevant previous year Bret Lee is a resident by virtue of fulfilling condition under section 6(1)(b). Hence, he has fulfilled condition under section 6(6)(i).
2. During seven previous years immediately preceding the relevant previous year (i.e., 2017-18), Bret Lee is in India for 700 days. Hence, he has not fulfilled the condition under section 6(6)(ii).

Illustration 5 Problem on Determination of Residential Status of Individuals

During the previous year 2017-18, a sailor has remained on ship for a private company owning ocean going ships as follows:

- (a) Outside the territorial waters of India for 183 days.
- (b) Inside the territorial waters of India for 182 days.

Is he considered to be resident or not for the assessment year 2018-19.

Solution:

According to section 6(1)(a), an individual can be a resident if he is in India for at least 182 days during the relevant previous year.

- 'Being in India' can be anywhere in India, including the territorial waters of India.
- In the relevant previous year 2017-18, the sailor is in the territorial waters of India for 182 days and hence has fulfilled condition under Section 6(1)(a).
- When at least one of the conditions under Section 6(1) is fulfilled, an individual becomes a 'resident'. Hence, in this case, the sailor is a '**resident in India**' for the assessment year 2018-19.

Illustration 6 Problem on Determination of Residential Status of Individuals

George, an American citizen, is appointed by a multi-national company to its branch in New Delhi in 2014. George has never been to India before this appointment. He arrives in Bombay on 15th April, 2014 and joins the New Delhi office on 20th April, 2014. His wife and children join him in India on 20th October, 2014. The company allotted him a leased residence for his stay. This residence is occupied by him from the beginning of October 2014.

On 10th February, 2015, he is transferred by his employer, on deputation basis, to be the regional chief to his employer's operations in South East Asia having headquarters in Hong Kong. He leaves New Delhi on 11th February, 2015 and arrives in Hong Kong on 12th February, 2015. George leaves behind his wife and children in India till 14th August 2016, when they leave along with him for Hong Kong. George had come to India earlier on 15th June, 2016 on two months' leave. The members of the family occupied the residence till the date of departure to Hong Kong.

At the end of the period of deputation, George is reposted to India and joins the New Delhi office of his employer as chief of Indian operations on 31st January 2018.

In what residential status will George be assessable, for assessment year 2018-19, to Income Tax in India?

4.12 • Income Tax-I

Solution:

Step 1: Calculation of Number of Days of Stay in India during different previous years

	APR	MAY	JUN	JUL	AUG	SEP	OCT	NOV	DEC	JAN	FEB	MAR	TOT
2017-2018	0	0	0	0	0	0	0	0	0	1	28	31	60
2016-2017	0	0	16	31	14	0	0	0	0	0	0	0	61
2015-2016													0
2014-2015	16	31	30	31	31	30	31	30	31	31	11	0	303
2013-2014													0
2012-2013													0
2011-2012													0
2010-2011													0
2009-2010													0
2008-2009													0
2007-2008													0

Notes:

1. While counting the number of days of stay, both date of arrival and date of departure has been considered.
2. The problem states that he comes to India on 15th June, 2016 for two months leave. It is assumed that he departs India on 14th August, 2016.

Step 2: Verification of Fulfillment of Conditions Under Section 6(1)

Condition Under Section 6(1)	Fulfilled or Not Fulfilled
(i) The Individual must be in India for at least 182 days during the relevant previous year (i.e., 2017-18)	Not Fulfilled
(ii) The Individual must be in India for at least 60 days during the relevant previous year (i.e., 2017-18) and at least 365 days during four previous years immediately preceding the relevant previous year (i.e., between 01.04.2013 and 31.03.2017)	Fulfilled Not Fulfilled

Since George has not fulfilled any of the conditions under section 6(1), he is a **non-resident** for the assessment year 2018-19.

Illustration 7 Problem on Determination of Residential Status of Individuals

In the above problem, what will be the difference in the residential status, if it is assumed that George is departing from India on 15th August, 2016 after two months leave in India?

Solution:*Step 1: Calculation of Number of Days of Stay in India during different previous years*

	APR	MAY	JUN	JUL	AUG	SEP	OCT	NOV	DEC	JAN	FEB	MAR	TOT
2017-2018	0	0	0	0	0	0	0	0	0	1	28	31	60
2016-2017	0	0	16	31	15	0	0	0	0	0	0	0	62
2015-2016													0
2014-2015	16	31	30	31	31	30	31	30	31	31	11	0	303
2013-2014													0
2012-2013													0
2011-2012													0
2010-2011													0
2009-2010													0
2008-2009													0
2007-2008													0

Step 2: Verification of Fulfillment of Conditions Under Section 6(1)

Condition Under Section 6(1)	Fulfilled or Not Fulfilled
(a) The Individual must be in India for at least 182 days during the relevant previous year (i.e., 2017-18)	Not Fulfilled
(b) The Individual must be in India for at least 60 days during the relevant previous year (i.e., 2017-18) and at least 365 days during four previous years immediately preceding the relevant previous year (i.e., between 01.04.2013 and 31.03.2017)	Fulfilled Fulfilled

Since George has fulfilled one of the conditions under section 6(1), he is a **resident** for the assessment year 2018-19.

Step 3: Verification of Fulfillment of Conditions under Section 6(6)

Condition Under Section 6(6)	Fulfilled or Not Fulfilled
(i) The Individual must be resident in India for at least 2 out of 10 previous years immediately preceding the relevant previous year (i.e., 2017-18)	Not Fulfilled
(ii) The Individual must be in India for at least 730 days during 7 previous years immediately preceding the relevant previous year (i.e., between 01.04.2010 and 31.03.2017)	Not Fulfilled

Since George, a resident individual, has not fulfilled any of the conditions under section 6(6), he is a **‘resident, but not ordinarily a resident’**.

Notes:

1. George becomes resident only for one previous year (2014-15) during 10 previous years immediately preceding the relevant previous year. Hence, he has not fulfilled condition under section 6(6)(i).
2. During 7 previous years immediately preceding the relevant previous year, George is in India for 365 days (i.e., 62 + 303). Hence, he has not fulfilled condition under section 6(6)(ii).

Illustration 8 Problem on determination of Residential Status of individuals

Mr. Bhaskar, born and brought up in India, joined a company in Bahrain on 1st October, 2013. He came back to India on 25th April, 2014 and went back on 25th May, 2014. He again came to India on 25th March, 2015 and left back on 22nd May, 2015. Due to acute illness, he came back to India on leave on 15th October, 2015 and joined back his duty on 1st August, 2017. He resigned his job on 1st January, 2018 and came back to India on 1st February, 2018. Determine the residential status for the assessment year 2018-19.

Solution:

Step 1: Calculation of Number of Days of Stay in India during different previous years

	APR	MAY	JUN	JUL	AUG	SEP	OCT	NOV	DEC	JAN	FEB	MAR	TOT
2017-2018	30	31	30	31	1	0	0	0	0	0	28	31	182
2016-2017													365
2015-2016	30	22	0	0	0	0	17	30	31	31	29	31	221
2014-2015	6	25	0	0	0	0	0	0	0	0	0	7	38
2013-2014	30	31	30	31	31	30	1	0	0	0	0	0	184
2012-2013													365
2011-2012													366
2010-2011													365
2009-2010													365
2008-2009													365
2007-2008													366

Notes:

1. While counting the number of days of stay, both the dates of arrival and departure have been considered.
2. The joining dates of company in Bahrain on 1st October, 2013 and 1st August, 2017, have been assumed as the date of departure from India.

Since, Bhaskar has fulfilled both the conditions under section 6(1), he is a **resident**, for the assessment year 2018-19.

Since Mr. Bhaskar is an Indian citizen who had left India for employment purposes, in condition under section (6)(1)(b), 182 days have been considered instead of 60 days.

Condition Under Section 6(6)	Fulfilled or Not Fulfilled
(i) The Individual must be resident in India for at least 2 out of 10 previous years immediately preceding the relevant previous year (i.e., 2017-18)	Fulfilled
(ii) The individual must be in India for at least 730 days out of 7 previous years immediately preceding the relevant previous year (i.e., between 01.04.2010 and 31.03.2017)	Fulfilled

Since Mr. Bhaskar has fulfilled both the conditions under section 6(6), he is a **resident and ordinarily a resident**, for the assessment year 2018-19.

Mr. Xavier, a German national, is appointed in India as a senior scientific officer on 01-04-2014. On 31st January, 2015 he goes to Iran on deputation for a period of three years but leaves his wife and children in India.

On May 1, 2016 he comes to India and takes with him his family on 30th June, 2016. He returns to India and joins his original job on 2nd February, 2018. Determine his residential status for the assessment year 2018-19.

Step 1: Calculation of Number of Days of Stay in India during different previous years

[illegible]

4.16 • Income Tax - I

	APR	MAY	JUN	JUL	AUG	SEP	OCT	NOV	DEC	JAN	FEB	MAR	TOT
2014-2015	30	31	30	31	31	30	31	30	31	31	0	0	306
2013-2014													0
2012-2013													0
2011-2012													0
2010-2011													0
2009-2010													0
2008-2009													0
2007-2008													0

Step 2: Verification of Fulfillment of Conditions Under Section 6(1)

Condition Under Section 6(1)	Fulfilled or Not Fulfilled
(a) The Individual must be in India for at least 182 days during the relevant previous year (i.e., 2017-18)	Not Fulfilled
(b) The Individual must be in India for at least 60 days during the relevant previous year (i.e., 2017-18) and at least 365 days during four previous years immediately preceding the relevant previous year (i.e., between 01.04.2013 and 31.03.2017)	Not Fulfilled Fulfilled

Since, Xavier has not fulfilled any condition under section 6(1), he is **non-resident**, for the assessment year 2018-19. The condition u/s 6(1)(b) is considered to be fulfilled only when both the parts of the condition are fulfilled. In this case, Xavier is not fulfilling the first part of the condition and hence, condition u/s 6(1)(b) is considered as 'not fulfilled'.

Note:

Since Xavier is a foreign national, 60 days have been considered in the condition under section 6(1)(b).

Illustration 10

Problem on determination of Residential Status of Individual being Indian citizen travelling as crew member of a ship

Mr. Narayan is an Indian citizen and a member of the crew of a Singapore bound Indian ship engaged in carriage of passengers in international traffic departing from Mangalore Port on 6th June, 2017. From the following details for Previous Year 2017-18, determine the residential status of Mr. Narayan for Assessment Year 2018-19, assuming that his stay in India in the last 4 years (preceding Previous Year 2017-18) is 400 days and last seven years (preceding Previous Year 2017-18) is 750 days:

Date entered into the Continuous Discharge Certificate in respect of joining the ship by Mr. Narayan	6 th June, 2017
Date entered into the Continuous Discharge Certificate in respect of signing off the ship by Mr. Narayan	9 th December, 2017

Solution:

Where an Indian citizen leaves India as a crew member of a ship, only condition u/s 6(1)(a) is applicable. Accordingly, if the individual is in India for 182 days or more during the relevant previous year, he will be a **Resident**.

In case of an **Indian citizen leaving India as a crew member of a foreign bound ship**, the period of stay of the individual in India shall **not include** – the period commencing from the date entered into the *Continuous Discharge Certificate* in respect of **joining the ship** for the *eligible voyage* and ending on the date entered into the *Continuous Discharge Certificate* in respect of **signing off by that individual from the ship** in respect of such voyage.

‘**Eligible Voyage**’ for this purpose means a voyage undertaken by a ship engaged in the carriage of passengers or freight in international traffic which has originated from any port in India and has its destination of any port outside India, or a voyage which has originated from any port outside India and has destination of any port in India.

In this case, Narayan is an Indian citizen and the voyage is an eligible voyage. Hence, for previous year 2017-18, the period between 6th June, 2017 and 9th December 2017 must not be included in calculating the number of days of stay in India.

Accordingly, **187 days** (i.e., June – 25 days, July – 31 days, August – 31 days, September – 30 days, October – 31 days, November – 30 days and December – 9 days) **must not be considered**. Consequently, Mr. Narayan is in India for only **178 days** (i.e., 365 days – 187 days) during previous year 2017-18.

According to condition under section 6(1)(a), an individual must be in India for 182 days during relevant previous year to be considered as ‘Resident’. Mr. Narayan’s stay being less than 182 days during previous year 2017-18, he is a **Non-resident**.

Note:

Since Mr. Narayan is a non-resident, his stay duration during previous years preceding previous year 2017-18 is not relevant.

SUMMARY

- ‘Residential Status’ refers to status of an assessee determined on the basis of his/her stay in India.
- For the purpose of determining residential status, assessees are classified into five categories viz., Individuals, Hindu Undivided Family, Companies, Firms and Others.
- In case of Individual assessees, residential status is basically classified into categories viz., Resident and Non-resident. Resident Individuals are further classified into two categories viz., Resident and Ordinarily a Resident **and** Resident, but not ordinarily a resident.
- An Individual is said to be ‘Resident and Ordinarily a Resident’ when he/she fulfills at least one condition under section 6(1) **and** both the conditions under section 6(6).
- An Individual is said to be ‘Resident, but not ordinarily a Resident’ when he/she fulfills at least one condition under section 6(1) **and**, either one or none of the conditions under section 6(6).
- An Individual is a ‘Non-resident’ when he/she does not fulfill any condition under section 6(1).

- Following are the two conditions specified under section 6(1):
 - (a) The individual must be in India for at least 182 days during the relevant previous year and
 - (b) The individual must be in India for at least 60 days during the relevant previous year, and for at least 365 days during 4 previous years immediately preceding the relevant previous year.
- In case of the condition u/s 6(1)(b), the number of days during relevant previous year must be considered as 182 days instead of 60 days in the following three cases:
 - In case of an Indian citizen leaving India for employment purposes;
 - In case of an Indian citizen leaving India as a crew member of a ship;
 - In case of a Person of Indian Origin coming on a visit to India or for permanent stay in India.
- Following are the two conditions specified under section 6(6):
 - (i) The individual must be resident in India for at least 2 out of 10 previous years immediately preceding the relevant previous year.
 - (ii) The individual must be in India for at least 730 days during 7 previous years immediately preceding the relevant previous year.

THEORY QUESTIONS

Section A Type Questions

1. What is 'residential status'?
2. What is the classification of assessee for the purpose of determining residential status?
3. What are the categories of residential status for an individual?
4. When is an individual said to be 'resident'?
5. When is an individual considered as 'non-resident'?
6. Who is a 'resident and ordinarily a resident' individual? **(Bangalore University, B.Com, December 2015)**
7. Who is a 'resident, but not ordinarily a resident' individual? **(Bangalore University, B.Com, December 2014)**
8. What are the conditions under section 6(1) for determining the basic residential status of an individual?
9. What are the exceptions for the condition under section 6(1)(b)?
10. Who is a 'person of Indian origin'?
11. List the conditions under section 6(6)?

Section B Type Questions

1. What are the provisions for determining residential status of an individual assessee?
2. List the conditions under section 6(1) and 6(6) applicable for determining residential status. Also list out the exceptions for the condition under section 6(1)(b).

Section C Type Questions

1. Explain in detail, determination of residential status of individual assessee.

EXERCISES

1. Mr. Abraham, a foreign citizen, left India for the first time on 20-05-2012. During the Previous Years 2017-18; 2016-17; 2015-16; 2014-15 and 2013-14, he visited India and stayed for a period of 181 days, 130 days, 165 days, 50 days and 19 days respectively. Determine his residential status for Assessment Year 2018-19.
(Ans: Non-resident)
2. Ms. Catherine, a foreign citizen, comes to India for the first time on 16-04-2015. During her stay in India up to 15-10-2017 she stays in Delhi up to 10-04-2017 and thereafter remains in Bangalore till her departure from India. Determine her residential status for Assessment Year 2018-19.
(Ans: Resident but not ordinarily resident)
3. Mr. Dominoz an Italian Citizen, comes to India for the first time on May 28, 2017 and stays up to January 15, 2018. Determine his residential status for Assessment Year 2018-19.
(Ans: Resident but not ordinarily resident)
4. Ms. Elizabeth, a foreign citizen, comes to India for the first time on 20-03-2017. On 1-09-2017 she leaves India for Nepal on a business trip and comes back on 26-02-2018. Determine her residential status for the Assessment Year 2018-19.
(Ans: Resident but not ordinarily resident)
5. Mr. Fernando, a foreign citizen, comes to India for the first time on 20-06-2017. On 6-09-2017 he leaves India for Bhutan on a business trip. He returns back to India on 1-1-2018. He maintains a dwelling house in India from the date of his arrival in India till 15-01-2018 when he leaves for Colombo. Determine his residential status for the Assessment Year 2018-19.
(Ans: Non-resident)
6. Mr. George, a foreign citizen, comes to India for the first time on 15-04-2013. During the Financial Years 2013-14; 2014-15; 2015-16; 2016-17 and 2017-18, he is in India for 130 days, 80 days, 13 days, 210 days and 75 days. Determine his residential status for Assessment Year 2018-19.
(Ans: Resident but not ordinarily resident)
7. Mr. Harry, a foreign citizen, comes to India for the first time on 22-06-2011 and up to 31-03-2018 he is in India as follows: 2011-12 - 182 days; 2012-13 - 360 days; 2013-14 - 365 days; 2014-15 - 365 days; 2015-16 - 365 days; 2016-17 - 59 days and 2017-18 - 92 days. Determine his residential status for Assessment Year 2018-19.
(Ans: Resident and ordinarily resident)
8. Mr. Irwin, a foreign citizen, not being a person of Indian origin leaves India for the first time in the last 20 years on 20-11-2015. During the calendar year 2016 he comes to India on 1-09-2016 for a period of 30 days. During the calendar year 2017 he does not visit India, but comes back to India on 16-01-2018. Determine his residential status for Assessment Year 2018-19.
(Ans: Resident and ordinarily a resident)
9. Mr. James, a foreign citizen, not being a person of Indian origin, leaves India for the first time in the last 12 years on 15-06-2015. During the calendar year 2016 he comes to India on 20-09-2016 for a period of 46 days. During the calendar year 2017 he does not come to India at all. He finally comes back on 31-01-2018 at 10:30 PM. Determine his residential status for Assessment Year 2018-19.
(Ans: Resident and ordinarily a resident')
10. Mr. Karol, a foreign citizen, comes to India during the Financial Year 2017-18 for 85 days. During the past 14 Financial Years he was in India as follows:

4.20 • Income Tax - I

Financial Year	No. of days of stay	Financial Year	No. of days of stay
2003-04	85 days	2010-11	59 days
2004-05	32 days	2011-12	59 days
2005-06	58 days	2012-13	55 days
2006-07	100 days	2013-14	62 days
2007-08	116 days	2014-15	135 days
2008-09	45 days	2015-16	146 days
2009-10	180 days	2016-17	55 days

Determine Mr. Karol's residential status for Assessment Year 2018-19.

(Ans: Resident but not ordinarily a resident)

11. Mr. Lawrence, a foreign citizen, comes to India during the Financial Year 2017-18 for 90 days. During the past 14 Financial Years he was in India as under:

Financial Year	No. of days of stay	Financial Year	No. of days of stay
2003-04	105 days	2010-11	48 days
2004-05	72 days	2011-12	53 days
2005-06	85 days	2012-13	45 days
2006-07	125 days	2013-14	62 days
2007-08	116 days	2014-15	125 days
2008-09	45 days	2015-16	155 days
2009-10	180 days	2016-17	65 days

Determine Mr. Lawrence's residential status for Assessment Year 2018-19.

(Ans: Resident but not ordinarily a resident)

12. Ms. Maria, a foreign citizen, comes to India during the Financial Year 2017-18 for 181 days. During the past 14 Financial Years she was in India as under:

Financial Year	No. of days of stay	Financial Year	No. of days of stay
2003-04	186 days	2010-11	59 days
2004-05	310 days	2011-12	55 days
2005-06	15 days	2012-13	120 days
2006-07	58 days	2013-14	180 days
2007-08	65 days	2014-15	85 days
2008-09	65 days	2015-16	58 days
2009-10	180 days	2016-17	180 days

Determine Ms. Maria's residential status for Assessment Year 2018-19.

(Ans: Resident and ordinarily a resident)

13. Mr. Nixon, a foreign citizen, comes to India during the Financial Year 2017-18 for 65 days. During the past 14 Financial Years he was in India as under:

Financial Year	No. of days of stay	Financial Year	No. of days of stay
2003-04	56 days	2010-11	16 days
2004-05	298 days	2011-12	45 days
2005-06	6 days	2012-13	110 days
2006-07	5 days	2013-14	180 days
2007-08	65 days	2014-15	65 days
2008-09	65 days	2015-16	10 days
2009-10	180 days	2016-17	120 days

Determine Mr. Nixon's residential status for Assessment Year 2018-19.

(Ans: Resident but not ordinarily a resident)

14. Mr. Dinesh, an Indian citizen, left India for the first time on 22-09-2017 to work as an officer of a company in Germany. Determine his residential status for the AY 2018-19.

(Ans: Non-Resident)

15. Ms. Eshwari an Indian citizen left India for the first time on 20-10-2017 to work as an officer of a company in USA. What is her residential status for the AY 2018-19?

(Ans: Resident and ordinarily a resident)

16. Mr. Suresh, aq Indian citizen left India for the first time on 22-09-2017 to participate in an exhibition at London. Determine his residential status for the AY 2018-19

(Ans: Resident and ordinarily a resident)

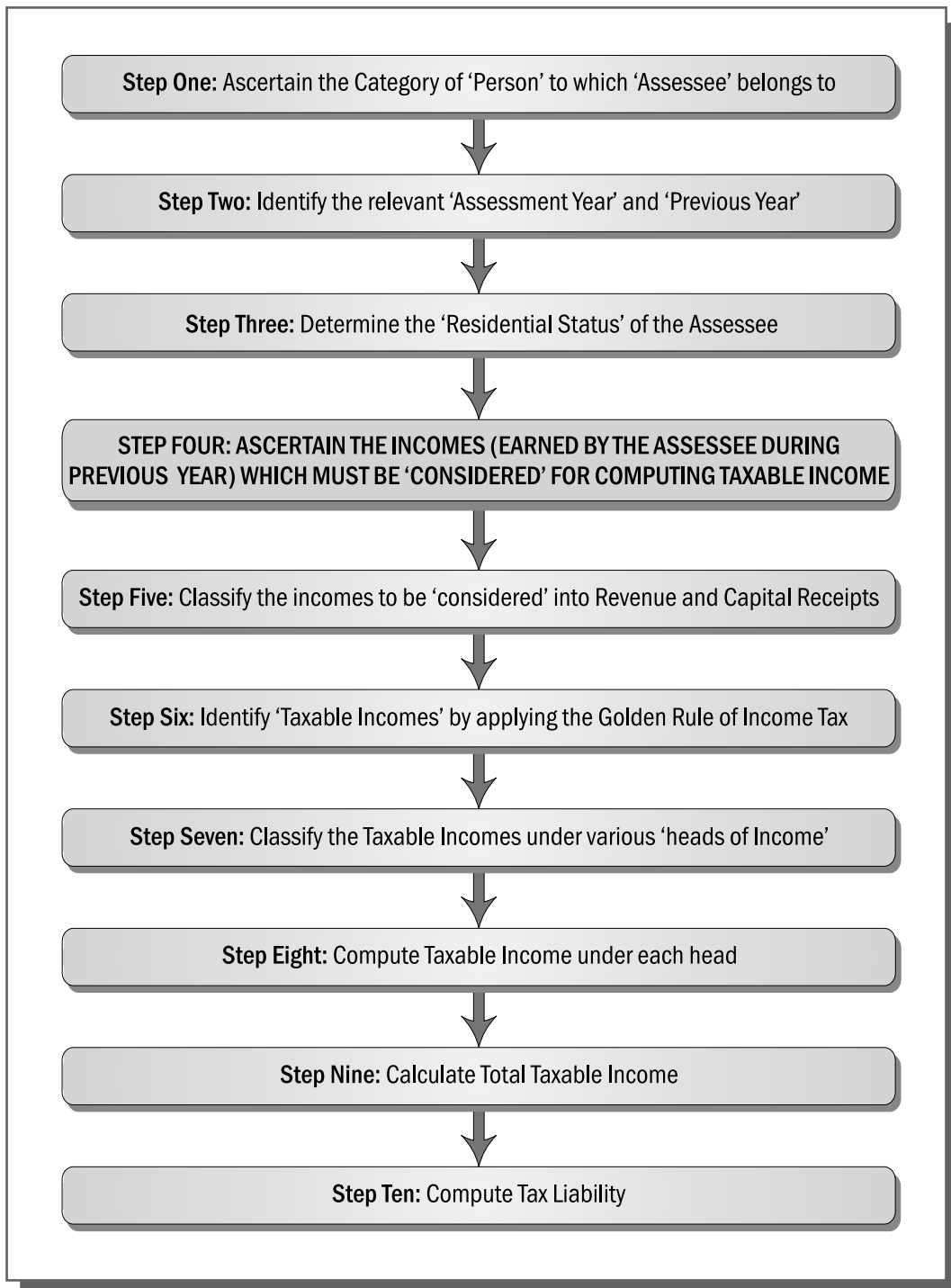
17. Mr. Vinay, a person of Indian origin came to India for the first time on 22-08-2017 for permanently staying in India. Determine his residential status for the AY 2018-19

(Ans: Resident but not ordinarily a resident)

18. Mr. Veeresh, a citizen of England came to India for the first time on 1/5/2011. He stayed in India without any break for 3 years and left for Singapore on 1/5/2014. He returned to India on 1/4/2015 and went back to England on 1/12/2015. He was pointed back to India on 20/1/2018. Determine his residential status for the AY 2018-19.

(Bangalore University, Nov/Dec 2014)

(Ans: Resident and ordinarily a resident)



- 5.1 Meaning of Incidence of Tax
- 5.2 Requirements for Determining the Incomes of the Assessee that must be Considered
- 5.3 Determination of Incomes that Must be Considered in Computing Taxable Income

- The purpose of determining residential status of an assessee is to identify – the incomes of the assessee (earned during relevant previous year) that must be considered – for computing taxable income. This chapter explains the procedure for identifying the incomes that must be considered.

5.1

Incidence of Tax refers to **identification of incomes** of the assessee that must be ‘considered’ for computing taxable income.

5.2

Identification of the incomes to be considered in computing taxable income is based on the following criteria:

1. Residential Status of the assessee.
2. Types of Income earned by the assessee.

Residential Status

The previous chapter has covered in detail the types and determination of residential status for individuals. The residential status of individuals is classified into the following categories:

5.4 • Income Tax-I

- (a) Resident and ordinarily a resident.
- (b) Resident, but not ordinarily a resident.
- (c) Non-resident.

Types of Income

For the purpose of determining the incomes of the assessee that must be 'considered', the incomes are classified into the following categories:

- (a) Indian Incomes
- (b) Foreign Incomes

5.2.1 Indian Income

An income is said to be 'Indian Income' when it is **either**,

- (i) Accrued in India, **or**
- (ii) Received in India, **or**
- (iii) Deemed to accrue in India, **or**
- (iv) Deemed to be received in India.

An income is said to **accrue in India** when the *source of Income* is in India. For example, salary received from an employer in Bangalore, Rent received for property let out in Lucknow, Profits made from business in Hyderabad, Profit made on sale of land in Cochin, Interest on Debentures of Reliance Industries Ltd., Interest on fixed deposit with Canara Bank, etc. When an income accrues in India, it can be considered as 'Indian income', irrespective of whether it is received in India or not.

An income is said to be **received in India** when the '**first receipt**' of the income is in India. An income, the first receipt of which is in India is 'Indian income', irrespective of whether it is accruing in India or not. For example, rent of property in Colombo sent to India by the tenant through cheque. The assessee deposits the cheque in his bank account in India. In this case, the first receipt of the rent is happening in India. And hence it becomes an Indian income. Where, the tenant deposits rent in the bank account of the assessee in Colombo and withdrawn by the assessee later, the first receipt of the rental income is not happening in India.

Incomes **deemed to accrue** in India means incomes not accruing in India, but treated as accruing in India. It includes the following:

- (i) Income from any activity or a ***business connection*** in India like business from a branch office in India, or any agent of a non-resident in India, or a subsidiary company in India etc.
- (ii) ***Salary*** payable by the ***Government of India*** to an ***Indian citizen*** for services rendered outside India.
- (iii) ***Interest*** payable by the Government of India **or** a person who is a resident in India, except where it is payable in respect of money borrowed and used for the purpose of business

or profession carried on outside India or earning any income from any source outside India **or** a person who is a non-resident in India provided interest is payable in respect of money borrowed and used for a business or profession carried on in India.

- (iv) **Royalty** payable by the Government of India **or** a person who is a resident in India, except where it is payable in respect of any right/information/property used for the purpose of a business or profession carried on outside India or earning any income from any other source outside India **or** a person who is a non-resident provided royalty is payable with respect of any right/information/property used for the purpose of the business or profession carried on in India or earning any income from any source in India.
- (v) **Fees** for technical services payable by the Government of India **or** a person who is a resident in India, except where services are utilized for a business or profession carried on outside India or earning any income from any source outside India **or** a person who is a non-resident provided fee is payable in respect of services for a business or profession carried on in India or earning any income from any source in India.

Income **deemed to be received** in India means incomes not received into the hands of the assessee, but treated as received. It includes:

- (i) Contribution made by the employer to the Recognised Provident Fund in excess of 12% of salary of the employee
- (ii) Interest credited to Recognised Provident Fund of the employee which is in excess of 9.5% p.a.
- (iii) Transferred balance from the Un-recognised Provident Fund to Recognised Provident Fund.
- (iv) Contribution made by the Central Government or any other employer, during the previous year, to the account of an employee under the Notified Contributory Pension Scheme, referred to in section 80CCD.

5.2.2 Foreign Income

An income is considered as foreign income, when the income **neither** accrues in India, **nor** is received in India.

DETERMINATION OF THE INCOMES THAT MUST BE CONSIDERED IN COMPUTING TAXABLE INCOME

5.3

The following table summarises the procedure for determining the incomes of the assessee that must be considered in computing taxable income:

5.6 • Income Tax-I

Income	Should the income be CONSIDERED in computing taxable income, if the assessee is-		
	Resident and ordinarily a resident	Resident but not ordinarily a resident	Non-resident
Indian Incomes			
1. Income accrued or deemed to accrue in India whether received in India or outside India.	YES	YES	YES
2. Income received or deemed to be received in India whether accrued in or outside India	YES	YES	YES
Foreign Incomes			
1. Income from business and profession carried outside India, but controlled from India.	YES	YES	NO
2. Income from business and profession carried outside India and controlled from outside India.	YES	NO	NO
3. Income from other sources (<i>i.e., income other than income from business or profession</i>) accrued and received outside India	YES	NO	NO
4. Income of earlier years (taxed or untaxed) brought into India during the previous year.	NO	NO	NO

Notes:

1. At this stage of assessment, we need to ascertain whether an income earned by the assessee during previous year, must be **CONSIDERED** or not. Whether such income is **taxable or not** cannot be ascertained at this stage.
2. The word 'received' given for an income can be considered as first receipt.
3. The word 'remitted' refers to payment made into India of an income received outside India. Hence, 'remitted' does not refer to the first receipt in India.
4. Unless otherwise stated, an income can be assumed to be received in the place of accrual.
5. Unless otherwise stated, the business carried on by assessee can be assumed to be controlled and managed in the place where the business is carried on.

Illustration 1 Problem on identifying the incomes of the assessee that must be considered in computing taxable income

Ascertain whether the following incomes can be considered in computation of taxable income of the assessee, when the assessee is:

- (a) Resident and ordinarily a resident.
- (b) Resident, but not ordinarily a resident.
- (c) Non-resident.

Incomes

1. Salary income for serving Infosys, Bangalore.
2. Salary income from Infosys, China.
3. Salary income from Google, USA, credited to assessee's HDFC Bank account in Bangalore.
4. Salary income from Wipro, Bangalore, credited to assessee's CitiBank in USA.
5. Salary income for service in London, received there, remitted to India.
6. Salary for working as Ambassador to the Government of India in London.
7. Rent from let-out property at Hyderabad.
8. Rent from let-out property at Colombo, paid by tenant directly in India through cheque.
9. Rent from let-out property at Sydney, deposited by tenant in assessee's bank account in Sydney.
10. Rent from let-out property in Patna transferred by tenant via net-banking to American Bank Account of the assessee in USA.
11. Income from business of the assessee in Trivandrum
12. Income from business of the assessee in Mumbai, profits received in London.
13. Income from business of the assessee in London, profits received in Kolkata.
14. Income from business of the assessee in New York controlled and managed from India.
15. Income from business of the assessee in Vienna, controlled and managed from there.
16. Income from business in Zurich, controlled from India – 60% of profits from the business is received in India.
17. Income from business in Goa – 75% of profits is received in New York.
18. Gain on sale of land located in Pune.
19. Gain on sale of land located in Islamabad.
20. Gain on sale of apartment in Miami for which consideration was received in India from the Buyer.
21. Gain on sale of jewellery in Dubai – 60% of profits were received in India.
22. Gain on sale of shares held for 3 years, through National Stock Exchange.
23. Agricultural income from land in Peenya, Bangalore.
24. Agricultural income from land located in Kenya.
25. Interest on deposits with Vijaya Bank, Bangalore.
26. Interest on deposit with Standard Chartered Bank, Nigeria.
27. Interest on Debentures of Tata Motors Ltd.
28. Interest on Securities issued by the Government of Germany.

5.8 • Income Tax - I

29. Interest on Debentures of a Private Limited Company in Italy, credited to assessee's bank account in Bangalore.
30. Dividends on Equity Shares of Hindustan Unilever Ltd.
31. Dividends on Shares of Apple Inc, credited to the bank account in USA.
32. Winnings from Sikkim Lottery.
33. Winnings from British Lottery.
34. Royalty income from Vittam Publications, based in Bangalore.
35. Royalty income from McMilan publishers, based in USA, for the sale of books in USA.
37. Income from letting out machinery for temporary use to a friend in Dubai, credited to bank account in Dubai, remitted to India.

Solution:

Statement showing whether the incomes should be 'considered' for assessment or not

Sl. No.	Income	Type of Income	Explanation	Should the income be considered in computing taxable income, if the assessee is–		
				Resident and ordinarily a resident	Resident but not ordinarily a resident	Non-resident
1.	Salary income for serving Infosys, Bangalore.	Indian	Salary accrues in the place of rendering service. Hence, the income is accruing in India.	Must be considered	Must be considered	Must be considered
2.	Salary income from Infosys, China.	Foreign	The income is accruing outside India and unless otherwise stated, is assumed to be received in the place of accrual.	Must be considered	Must not be considered	Must not be considered
3.	Salary income from Google, USA, credited to assessee's HDFC Bank account in Bangalore.	Indian	The first receipt of the income is in India and hence it becomes an Indian income.	Must be considered	Must be considered	Must be considered
4.	Salary income from Wipro, Bangalore, credited to assessee's CitiBank in USA.	Indian	Salary accrues in the place of rendering service. Hence, the income is accruing in India.	Must be considered	Must be considered	Must be considered

Sl. No.	Income	Type of Income	Explanation	Should the income be considered in computing taxable income, if the assessee is—		
				Resident and ordinarily a resident	Resident but not ordinarily a resident	Non-resident
5.	Salary income for service in London, received there remitted here	Foreign	Income accrued and received outside India.	Must be considered	Must not be considered	Must not be considered
6.	Salary for working as Ambassador to the Government of India in London	Indian	Salary is paid by the Government of India to an Indian citizen for rendering service outside India. It is an income 'deemed to accrue in India' and hence an Indian income.	Must be considered	Must be considered	Must be considered
7.	Rent from let-out property at Hyderabad	Indian	Source of income being in India, the income is accruing in India.	Must be considered	Must be considered	Must be considered
8.	Rent from let-out property at Colombo, paid by tenant directly in India through cheque	Indian	The income is directly received in India (i.e., the first receipt is in India). Hence, it is an Indian income.	Must be considered	Must be considered	Must be considered
9.	Rent from let-out property at Sydney, deposited by tenant in assessee's bank account in Sydney	Foreign	Income is accruing and received outside India.	Must be considered	Must not be considered	Must not be considered
10.	Rent from let-out property in Patna transferred by tenant via net-banking to American Bank A/c in USA	Indian	The property being located in India and hence, the income is accruing in India.	Must be considered	Must be considered	Must be considered
11.	Income from business of the assessee in Trivandrum	Indian	The business is located in India and hence, the income is accruing in India.	Must be considered	Must be considered	Must be considered

5.10 • Income Tax - I

Sl. No.	Income	Type of Income	Explanation	Should the income be considered in computing taxable income, if the assessee is—		
				Resident and ordinarily a resident	Resident but not ordinarily a resident	Non-resident
12.	Income from business of the assessee in Mumbai, profits received in London	Indian	The business is carried out in India and hence the income is accruing in India.	Must be considered	Must be considered	Must be considered
13.	Income from business of the assessee in London, profits received in Kolkata	Indian	The profits are received in India, and hence it is an Indian income.	Must be considered	Must be considered	Must be considered
14.	Income from business of the assessee in New York controlled and managed from India	Foreign	Income accrued and received outside India.	Must be considered	Must be considered	Must not be considered
15.	Income from business of the assessee in Vienna, controlled and managed from there	Foreign	Income accrued and received outside India.	Must be considered	Must not be considered	Must not be considered
16.	Income from business in Zurich, controlled from India – 60% of profits from the business is received in India	60% is Indian Income, and 40% is Foreign Income	To the extent income is received in India, it is Indian income. The business is controlled from India.	100% of profits must be considered	100% of profits must be considered	60% of profits must be considered
17.	Income from business in Goa – 75% of profits is received in New York	Indian	Income is accrued in India, since the business is carried out in India.	Must be considered	Must be considered	Must be considered
18.	Gain on sale of land located in Pune	Indian	Income is accrued in India, since the land sold is in India.	Must be considered	Must be considered	Must be considered
19.	Gain on sale of land located in Islamabad	Foreign	Income accrued outside India and assumed to be received at the place of accrual.	Must be considered	Must not be considered	Must not be considered

Sl. No.	Income	Type of Income	Explanation	Should the income be considered in computing taxable income, if the assessee is–		
				Resident and ordinarily a resident	Resident but not ordinarily a resident	Non-resident
20.	Gain on sale of apartment in Miami for which consideration was received in India from the Buyer	Indian	Income is received in India	Must be considered	Must be considered	Must be considered
21.	Gain on sale of jewellery in Dubai – 60% of profits were received in India	60% is Indian Income, and 40% is Foreign Income	To the extent income is received in India, it is Indian income.	100% of profits must be considered	60% of profits must be considered	60% of profits must be considered
22.	Gain on sale of shares held for 3 years through National Stock Exchange (See Note 1)	Indian	Income is accrued and received in India.	Must be considered	Must be considered	Must be considered
23.	Agricultural income from land in Bangalore (See Note 1)	Indian	Income is accrued and received in India.	Must be considered	Must be considered	Must be considered
24.	Agricultural income from land located in Kenya	Foreign	Income accrued and received outside India.	Must be considered	Must not be considered	Must not be considered
25.	Interest on deposits with Vijaya Bank, Bangalore	Indian	Income accrued in India.	Must be considered	Must be considered	Must be considered
26.	Interest on deposit with Standard Chartered Bank, Nigeria	Foreign	Income accrued and received outside India.	Must be considered	Must not be considered	Must not be considered
27.	Interest on Debentures of Tata Motors Ltd.	Indian	Income accrued and received in India.	Must be considered	Must be considered	Must be considered
28.	Interest on Securities issued by the Govt. of Germany	Foreign	Income accrued and received outside India.	Must be considered	Must not be considered	Must not be considered

5.12 • Income Tax-I

Sl. No.	Income	Type of Income	Explanation	Should the income be considered in computing taxable income, if the assessee is–		
				Resident and ordinarily a resident	Resident but not ordinarily a resident	Non-resident
29.	Interest on Debentures of a Private Limited Company in Italy, credited to assessee's bank a/c in Bangalore	Indian	Income received in India.	Must be considered	Must be considered	Must be considered
30.	Dividends on Equity Shares of Hindustan Unilever Ltd. (See Note 1)	Indian	Income accrued and received in India.	Must be considered	Must be considered	Must be considered
31.	Dividends on Shares of Apple Inc, credited to the bank a/c in USA	Foreign	Income accrued and received outside India.	Must be considered	Must not be considered	Must not be considered
32.	Winnings from Sikkim Lottery	Indian	Income accrued and received in India.	Must be considered	Must be considered	Must be considered
33.	Winnings from British Lottery	Foreign	Income accrued and received outside India.	Must be considered	Must not be considered	Must not be considered
34.	Royalty income from Vittam Publications-based in Bangalore	Indian	Income accrued and received in India.	Must be considered	Must be considered	Must be considered
35.	Royalty income from Mc Milan publishers, based in USA, for the sale of books in USA	Foreign	Income accrued and received outside India.	Must be considered	Must not be considered	Must not be considered
36.	Income from letting out machinery for temporary use to a friend in Dubai, credited to bank account in Dubai, remitted to India	Foreign	Income accrued and received outside India.	Must be considered	Must not be considered	Must not be considered

Notes:

1. At this stage, the effort is to ascertain whether an income must be considered or not in computing taxable income, and not whether it is **taxable or exempt**.

2. Unless otherwise stated, an income is assumed to be received in the place of accrual.

SUMMARY

- Incidence of tax refers to identification of incomes that must be considered in computing taxable income of an assessee. It involves deciding on which of assessee's incomes earned by him during the relevant previous year, must be considered in computing taxable income.
- For the purpose of identifying the incomes that must be considered in computing taxable income, two components are required viz., the residential status of the assessee and the type of income earned by the assessee.
- Type of income, in this case, is classification of income on the basis of the source from which income is earned. On this basis, incomes are of two types viz., Indian incomes and Foreign incomes.
- Indian incomes refer to incomes which are either **earned** in India or **received** in India.
- Incomes which are neither earned nor received in India are **foreign incomes**.
- In case of individuals who are 'residents, and ordinarily residents', all Indian and foreign incomes earned during previous year must be considered for computing taxable income.
- In case of 'non-resident' individuals, only Indian Incomes earned during previous year must be considered.
- In case of individuals who are 'residents, but not ordinarily residents', all Indian incomes and 'income from business or profession outside India, but controlled from India' must be considered.

THEORY QUESTIONS

Section A Type Questions

1. What is 'incidence of tax'?
2. What are the requirements or inputs for ascertaining incidence of tax?
3. State the different types of incomes for the purpose of ascertaining incidence of tax.
4. What is an 'Indian Income'?
5. When is an income said to accrue in India?
6. When is an income 'deemed to accrue in India'? Give any two situations.
7. When is an income 'deemed to be received'?
8. How do you treat an income as Indian Income or Foreign Income?

(Bangalore University, B.Com., December 2015)

Section B Type Questions

1. What is Incidence of Tax? Explain the consideration of foreign incomes based on residential status.
2. Explain the meaning of 'income deemed to accrue in India'.

Section C Type Questions

1. Explain in detail the provisions relating to incidence of tax, according to the provisions of Income Tax Act, 1961.

EXERCISES

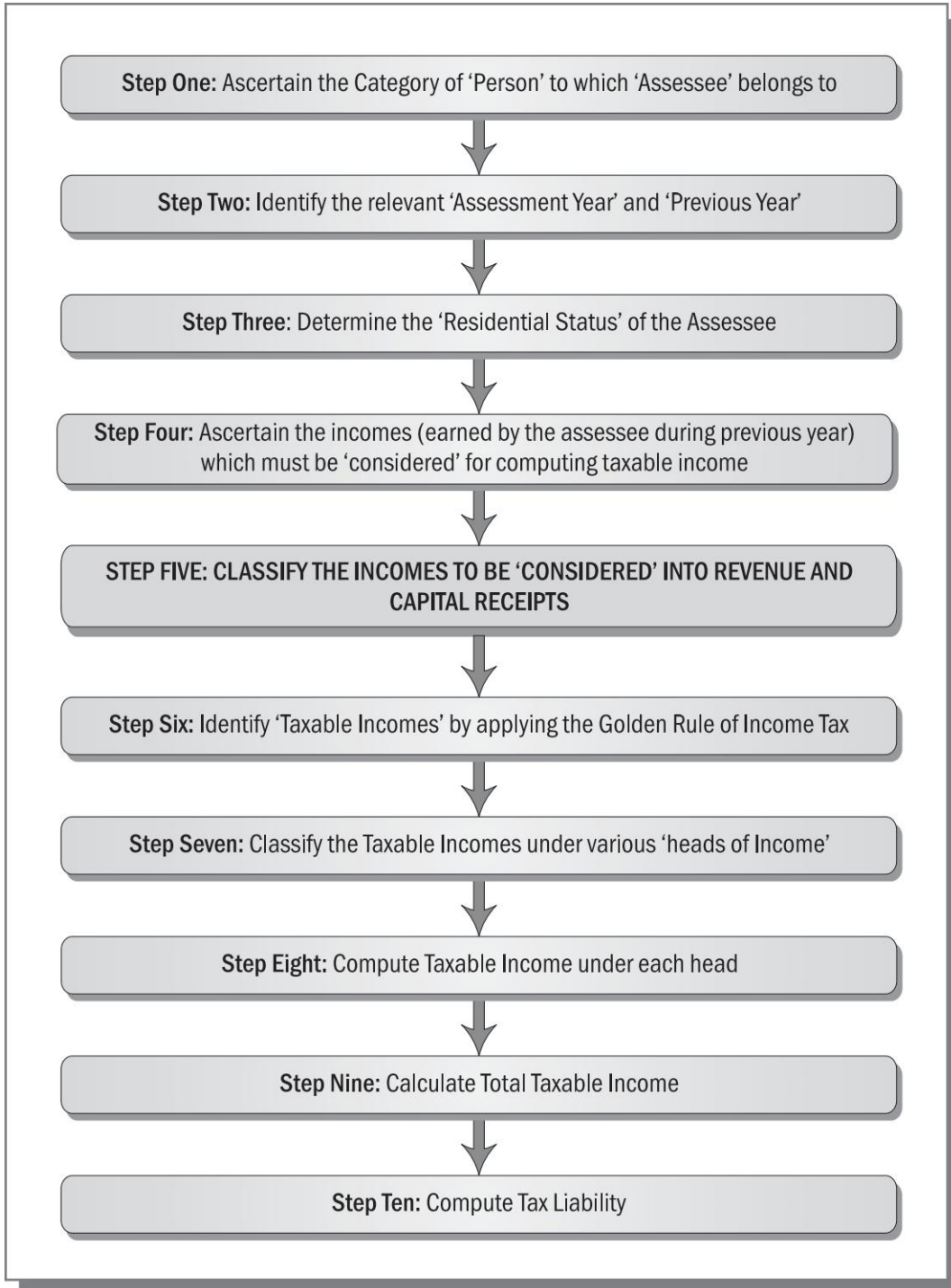
Identify the incomes that must be considered in computing taxable income of Mr. Jaikumar, if he is—

- (a) A resident, and ordinarily a resident.
 - (b) A resident, but not ordinarily a resident.
 - (c) Non-resident.
1. Salary income from Tata Sons Ltd., New Delhi.
 2. Rental income from a let-out property at Sydney.
 3. Income from business in Vienna, controlled from India.
 4. Income from Fixed Deposit with State Bank of India.
 5. Income from Fixed Deposit with Bank of America, New York.
 6. Income from private consulting at Bangalore, credited to his account in New York.
 7. Income earned during 2014-15 in Sydney, brought to India during 2017-18.
 8. Profit on sale of house property in Cape Town, 70% of which was paid in India.

(Ans)

Sl. No.	If Mr. Jaikumar is—		
	Resident and ordinarily a resident	Resident, but not ordinarily a resident	Non-resident
1	Must be considered	Must be considered	Must be considered
2	Must be considered	Must not be considered	Must not be considered
3	Must be considered	Must be considered	Must not be considered
4	Must be considered	Must be considered	Must be considered
5	Must be considered	Must not be considered	Must not be considered
6	Must be considered	Must be considered	Must be considered
7	Must not be considered	Must not be considered	Must not be considered
8	100% Must be considered	70% Must be considered	70% Must be considered

[Hint: Unless otherwise stated, income is assumed to be received in the place of accrual]



6

Revenue and Capital Receipts

CHAPTER OVERVIEW

- 6.1 Meaning
- 6.2 Difference between Revenue Receipts and Capital Receipts

The **next step** in making assessment is to classify the incomes that must be 'considered' into revenue receipts and capital receipts. This chapter explains the difference between revenue and capital receipts.

MEANING

6.1

According to English Dictionary, 'Revenue' means "the return, yield, or profit of any lands, property or any other important source of income; that which comes in to one as a return from property or possessions; income from any source" and 'Capital' means "accumulated wealth employed reproductively".

DIFFERENCE BETWEEN REVENUE RECEIPTS AND CAPITAL RECEIPTS

6.2

The distinction between revenue and capital receipts is different for accounting perspective and for tax perspective.

From the taxation perspective, the following are the differences between Revenue and Capital Receipts:

1. A receipt on account of circulating capital is revenue receipt, whereas a receipt on account of fixed capital is capital receipt.
2. A receipt **from a source** is revenue receipt, whereas a receipt **in lieu of the source** of income is capital receipt.

6.4 • Income Tax - I

Notes:

- (a) Whether a receipt is lump sum or periodical is not relevant in classifying the receipt into revenue or capital.
- (b) Whether a receipt is regular or irregular is not relevant in classifying the receipt into revenue or capital.
- (c) The second point of distinction is most crucial and relevant for classification of assessee's incomes into revenue or capital.

Illustration 1 Problem on classification of incomes into revenue receipts and capital receipts

Classify the following incomes of the assessee into revenue receipts and capital receipts:

1. Salary income from Reliance Ltd.
2. Retrenchment compensation from NGEF Ltd.
3. Voluntary retirement compensation from Canara Bank
4. Gratuity received on retirement from HAL
5. Pension received after retirement
6. Rental income from property at Bangalore
7. Profit on sale of property at Goa
8. Profit from the business of textiles
9. Compensation received for cancellation of 'dealership' in Titan Watches
10. Royalty from books, received in lump sum
11. Amount received on relinquishment of copyrights
12. Interest on Debentures
13. Profit on sale of shares
14. Lottery winnings
15. Interest on Bank Deposits
16. Insurance compensation received on theft of vehicle
17. Amount received on maturity of life insurance policy

Solution:

Sl. No.	Income	Nature of Receipt
1.	Salary income from Reliance Ltd.	Revenue (being receipt from the source of 'employment')
2.	Retrenchment compensation from NGEF Ltd.,	Capital (being a receipt in lieu of 'employment' source)
3.	Voluntary retirement compensation from Canara Bank	Capital (being a receipt in lieu of 'employment' source)

Sl. No.	Income	Nature of Receipt
4.	Gratuity received on retirement from HAL	Revenue (being receipt from the source of 'employment')
5.	Pension received after retirement	Revenue (being receipt from the source of 'employment')
6.	Rental income from property at Bangalore	Revenue (being receipt from the source of 'House Property')
7.	Profit on sale of property at Goa	Capital (being receipt in lieu of 'property' source)
8.	Profit from the business of textiles	Revenue (being receipt from the source of 'business')
9.	Compensation received for cancellation of 'dealership' in Titan Watches	Capital (being receipt in lieu of 'business' source – i.e., the dealership)
10.	Royalty from books, received in lump sum	Revenue (being receipt from the source of 'copyrights') It is immaterial, whether the receipt is received in lump sum or otherwise.
11.	Amount received on relinquishment of copyrights	Capital (being receipt in lieu of the source of 'copyrights')
12.	Interest on Debentures	Revenue (being receipt from the source of 'investments')
13.	Profit on sale of shares	Capital (being receipt in lieu of 'investment' source)
14.	Lottery winnings	Revenue (being receipt from the source of 'investment in Lottery Scheme') (There cannot be a possibility of receipt in lieu of source, in this case. Further, the fact that the receipt may be one time and may or may not occur, is immaterial in classifying the income into revenue or capital)
15.	Interest on Bank Deposits	Revenue (being receipt from the source of 'investment in Bank')
16.	Insurance compensation received on theft of vehicle	Capital (being receipt in lieu of asset)
17.	Amount received on maturity of life insurance policy	Capital (being receipt in lieu of maturity of the policy)

SUMMARY

- After identifying the incomes that must be considered in computing taxable income, the next step in making assessment is classifying the 'incomes which must be considered' into revenue receipts and capital receipts.
- Revenue receipts refer to 'incomes received from a source', while Capital receipts refer to 'incomes received in lieu of a source'.

THEORY QUESTIONS

Section A Type Questions

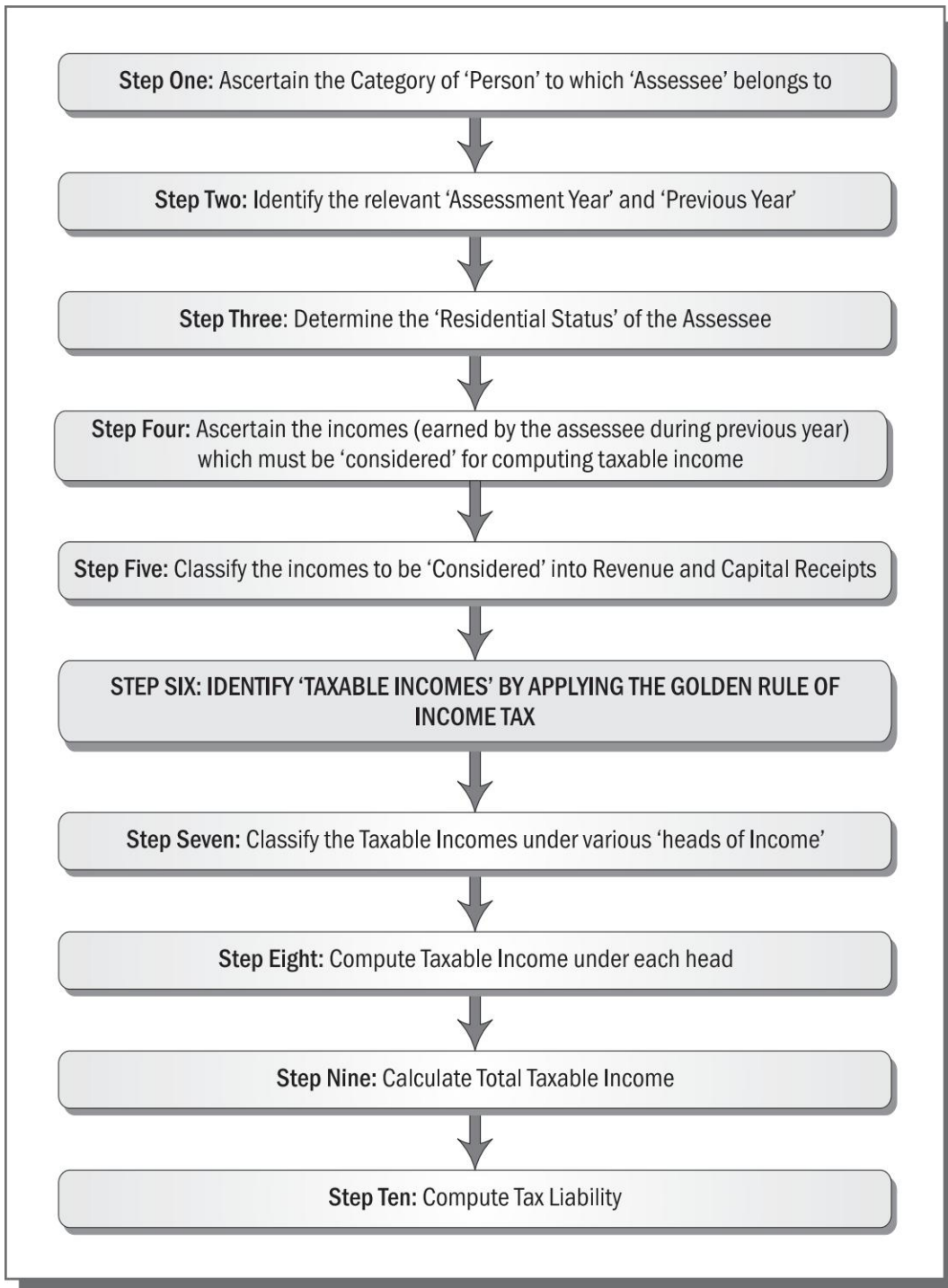
1. State the different types of receipts.
2. What is the meaning of the term 'capital receipt'?
3. What is the meaning of the term 'revenue receipt'? (**Bangalore University, B.Com., December 2015**)
4. State the differences between 'revenue receipts' and 'capital receipts' from tax perspective.
5. Give any five examples for revenue receipts.
6. Give any five examples for capital receipts.

EXERCISES

Classify the following incomes into Revenue Receipts and Capital Receipts

1. Compensation received for termination of contract by Supplier of Raw materials.
2. Amount received on maturity of Life Insurance Policy.
3. Accumulated balance of Provident Fund withdrawn.
4. Interest on Savings Bank Account credited to the Account.
5. Amount received on maturity of Fixed Deposit.
6. Dividend income from Google Inc.
7. Amount received on sale of shares of Bharat Dynamics Ltd.

(Ans: (1) Capital (2) Capital (3) Capital (4) Revenue (5) Capital (6) Revenue (7) Capital)



7

Exempted and Taxable Incomes

CHAPTER OVERVIEW

- 7.1 Introduction
- 7.2 Incomes Exempt under Section 10
- 7.3 Income Exempt under Section 10(1)

- In the process of making assessment, the **next**
- **step** is to identify the taxable incomes among
- those incomes earned by the assessee, which
- must be 'considered' in computing taxable income.
- This chapter explains the rule for identification of
- taxable incomes of the assessee

7.1

INTRODUCTION

Based on the nature of income earned by the assessee (i.e., whether revenue or capital), the next step in the process of making assessment is to identify whether the incomes are taxable or exempt.

The taxability of an income is ascertained with the help of the **Golden Rule of Income Tax**, which states that—

**ALL REVENUE RECEIPTS ARE TAXABLE UNLESS SPECIFICALLY EXEMPT
AND
ALL CAPITAL RECEIPTS ARE EXEMPT UNLESS SPECIFICALLY TAXABLE**

Where an income earned by an assessee has to be 'considered' and if such income happens to be revenue in nature, it is taxable in case it is not specifically exempt. The list of **exempted incomes** is given under **section 10** of the Income Tax Act.

Where an income earned by an assessee has to be 'considered' and if such income happens to be capital in nature, it is taxable only if so specified under any section of the Act. The list of taxable capital receipts is spread across the Act.

INCOMES EXEMPT UNDER SECTION 10

7.2

The list of exempted incomes has been summarized in the table given below. Exemptions applicable from and amendments effective from Assessment Year 2018-19 have been given in **bold**:

Section Number	Income
10(1)	Agricultural income
10(2)	Amount received as share of income from the HUF
10(2A)	Amount received as share of profits from the firm by a partner of a partnership firm
10(4)	Interest on notified bonds and securities issued to Non-residents
10(4)(ii)	Interest on Non-resident (External) Account
10(4B)	Amount received as interest from prescribed savings certificates by a non-resident Indian citizen or a person of Indian origin
10(5)	Leave travel concession from employer
10(6)	Remuneration received by individuals who are not citizens of India
10(6)(i)	Passage moneys/value of free or concessional passage received by a salaried individual, not being a citizen of India
10(6)(ii)	Remuneration of officials of an Embassy, high commission, legation, commission, consulate or trade representation of a foreign state.
10(6)(vi)	Remuneration of an employee of foreign enterprise for services rendered during his stay in India
10(6)(viii)	Remuneration of non-resident employees for services on a foreign ship
10(6) (xi)	Remuneration of an Indian citizen as an employee of the Government of a foreign state
10(6A)	Tax paid on Royalty or fees for technical services of a foreign company
10(6B)	Tax paid on income for a non-resident non-corporate assessee or a foreign company
10(6BB)	Tax paid on income derived from leasing an aircraft or an aircraft engine to an Indian company by a Government of a foreign state or a foreign enterprise
10(6C)	Royalty or fees for technical services received by foreign companies notified by the Central Government
10(7)	Allowances and perquisites paid or allowed by the Government of India to a citizen of India for services rendered outside India
10(8)	Remuneration or any other income accruing or arising outside India to an individual engaged in duties in connection with any co-operative technical assistance programs and projects
10(8A)	Any remuneration received from an international organization for services in India by an individual who is not an Indian citizen or an Indian citizen who is not ordinarily resident

Section Number	Income
10(8B)	Any remuneration received from an Individual (as mentioned in 10(8A) above for services in India by an individual who is not an Indian citizen or an Indian citizen who is not ordinarily resident
10(9)	Any income accruing or arising outside India to a member of the family of the individual mentioned in sections 10(8), 10(8A) and 10(8B)
10(10)	Gratuity
10(10A)	Commuted pension
10(10AA)	Leave encashment
10(10B)	Retrenchment Compensation
10(10BB)	Amount received under the Bhopal Gas Leak Disaster (Processing of Claims) Act, 1985
10(10BC)	Compensation received or receivable on any disaster
10(10C)	Compensation for voluntary retirement
10(10CC)	Tax on non-monetary perquisites
10(10D)	<p>Sum received under a life insurance policy if the premium payable for any year does not exceed 10% of capital sum assured for policies issued on or after 01.04.2012. (The limit is 20% of capital sum assured for policies issued before 01.04.2012).</p> <p>The limit has been increased to 15 per cent of capital sum assured (if policy is issued on or after 01.04.2013) for insurance on the life of any person who is–</p> <ul style="list-style-type: none"> • a person with disability or a person with severe disability as referred to in section 80U, or • suffering from disease or ailment as specified in the rules made under section 80DDB
10(11)	Payments received from Statutory Provident Fund
10(11A)	Interest on Deposit under Sukanya Samriddhi Account Rules
10(12)	Accumulated balance in Recognized Provident Fund
10(12A)	Payment from National Pension System Trust to an employee on closure of account or his opting out of the pension scheme referred to in Section 80CCD to the extent it does not exceed 40 per cent of the total amount payable to him at the time of closure or his opting out of the scheme
10(12B)	Any payment from National Pension System Trust to an employee under the Pension Scheme referred to in section 80CCD, on partial withdrawal made out of his account in accordance with the terms and conditions specified under the Pension Fund Regulatory and Development Authority Act, 2013 and the regulations made there under, shall be exempt from tax to the extent it does not exceed 25% of the amount of contributions made by him
10(13)	Payment from approved superannuation fund or transfer to National Pension Scheme
10(13A)	House Rent Allowance

7.6 • Income Tax-I

Section Number	Income
10(14)	Prescribed Allowances
10(15)	Interest income on certain securities
10(15A)	Income derived from leasing an aircraft or an aircraft engine to an Indian company by a Government of a foreign state or a foreign enterprise
10(16)	Scholarships to meet the cost of education
10(17)	Allowances received by a Member of Parliament or any State Legislature or any Committee thereof
10(17A)	Awards received in cash or in kind from Central or State Government or any other body approved by the Central Government
10(18)	Pension or Family pension received by a Central or State Government Employee who was awarded 'Param Vir Chakra' or the 'Maha Vir Chakra' or the 'Vir Chakra' or such other gallantry award
10(19)	Family pension received by family members of armed forces personnel killed in action
10(19A)	Annual value of a palace in the occupation of a ruler
10(20)	Income from House Property, Capital Gains or income from other sources or income from trade or business of a local authority
10(21)	Any income of a scientific research association, research associations undertaking research in social science or statistical research
10(22B)	Any income of Press Trust of India, New Delhi (from Assessment Year 2016-17 to Assessment Year 2018-19)
10(23)	Income of notified sports or games institutions
10(23A)	Any income of an association or institution established in India having as its object the control, supervision, regulation or encouragement of the profession of law, medicine, accountancy, engineering or architecture or other specified profession, other than income from house property, income for rendering specific services and interests or dividends on investments
10(23AA)	Any income received on behalf of any Regimental Fund or Non-public Fund established by the armed forces
10(23AAA)	Any income received on behalf of a fund established for purposes notified by the Board for welfare of employees or their dependents
10(23AAB)	Any income received on behalf of a fund established by LIC under a pension scheme duly approved by appropriate authority
10(23B)	Any income of a Society or Public Charitable Trust for development of Khadi and Village Industries
10(23BB)	Any income of Khadi and Industries Board
10(23BBA)	Income of statutory bodies for administration of public charitable trust
10(23BBB)	Interests, dividends or capital gains from investments received by European Economic Community

Section Number	Income
10(23BBC)	Income of SAARC Fund
10(23BBD)	Income of Secretariat of Asian Organisation of Supreme Audit Institution
10(23BBE)	Income of Insurance Regulatory and Development Authority
10(23BBF)	Income of North Eastern Development Financial Corporation Limited
1023(BBG)	Income of Central Electricity Regulatory Commission
10(23BBH)	Income of Prasar Bharati (Broadcasting Corporation of India)
10(23C)	Income of certain National Funds, Educational Institutions, Universities and Hospitals which exist solely for educational purposes or solely for philanthropic purposes, and not for the purpose of profit and which are wholly or substantially financed by the Government for any previous year, if the Government grant to such University or other educational institution, hospital or other institution exceeds such percentage of the total receipts including voluntary contributions, as may be prescribed, of such University, or other educational institution, hospital or other institution, as the case may be, during the relevant previous year. From Assessment Year 2016-17, Income of The Swachh Bharath Kosh and The Clean Ganga Fund are exempt from tax under this section.
10(23D)	Income of any registered Mutual Fund
10(23DA)	Income from the activity of securitization of Securitisation Trusts
10(23EA)	Income of Investor Protection Fund
10(23EB)	Income of Credit Guarantee Fund Trust for small industries
10(23EC)	Specified income of Investor Protection Fund set up by Commodity Exchanges
10(23ED)	Income, by way of contributions received from a depository, of Investor Protection Fund set up in accordance with the regulations made under the SEBI Act and the Depositories Act, by a depository, as the Central Government may, by notification in the Official Gazette, specify in this behalf
10(23EE)	Specified Income of Core Settlement Guarantee Fund set up by a Recognised Clearing Corporation
10(23FB)	Income of Venture Capital Fund or company from investment in a venture capital undertaking
10(23FBA)	Income of Investment Fund
10(23FBB)	Income of Unit Holders of Investment Fund
10(23FC) 10(23FCA) 10(23FD)	Income of Business Trusts
10(23G)	Dividends, interest or long-term capital gains of Infrastructure Capital Company or fund or a Co-operative bank
10(24)	Income from house property and income from other sources of a Registered Trade Union

7.8 • Income Tax - I

Section Number	Income
10(25)	Interest on securities of approved provident fund
10(25A)	Any income of Employees State Insurance Fund
10(26)	Income of a member of a Scheduled Tribe
10(26A)	Income of resident of Ladakh
10(26AAA)	Income received by Sikkamese
10(26AAB)	Income of Agricultural Produce Marketing Committee or Board
10(26B)	Income of a body for promoting interest of Scheduled Castes/Tribes
10(26BB)	Income of National Minorities Development and Finance Corporation
10(26BBB)	Income of ex-serviceman corporations
10(27)	Income of co-operative societies promoting the interest of members of Scheduled Castes/Tribes
10(29A)	Exemption of Commodity Boards and Authorities from Income Tax
10(30)	Subsidy from Tea Board
10(31)	Subsidy received by planters
10(32)	Income of minor, when clubbed with parent's income
10(33)	Capital gain on transfer of US 64
10(34)	Dividends from domestic companies up to ₹10,00,000. Excess dividend over and above ₹10,00,000 is chargeable in case of Resident Individual, Resident HUF and Resident Firms at the rate of 10% plus applicable Surcharge and Cess
10(34A)	Income arising to a shareholder in respect of buy-back of unlisted shares by the company, provided additional income tax is payable on distributed income under section 115QA by the company opting for buy-back of unlisted shares
10(35)	Income from units of UTI and notified Mutual Funds
10(35A)	Income received by an investor from a securitization trust on or before 31st May 2016
10(37)	Capital gain on compulsory acquisition of urban agriculture land
10(37A)	An Individual or a Hindu Undivided Family who was the owner of land as on 2nd June 2014, and has transferred the land under the land pooling scheme notified under the provisions of Andhra Pradesh Capital Region Development Authority Act, 2014, shall be exempt from tax on capital gains arising from transfer of land or building or both, or sale of Land Pooling Ownership Certificates.
10(38)	Long-term capital gains on transfer of equity shares/units liable for payment of Securities Transaction Tax, and Long-term capital gain arising from transaction undertaken in foreign currency on a recognised stock exchange located in an International Financial Services Centre even when securities transaction tax is not paid in respect of such transactions
10(39)	Specified income from international sporting event held in India
10(40)	Grant etc., received by a subsidiary company from its holding company engaged in the business of generation, etc., of distribution of power

Section Number	Income
10(41)	Capital gain on transfer of an asset of an undertaking engaged in the business of generation etc., of power
10(42)	Body or Authority – Agreement between two countries
10(43)	Any sum received as loan under Reverse Mortgage Scheme
10(44)	Any income received by a person on behalf of the New Pension Scheme Trust
10(45)	Perquisites to chairman or retired chairman or any member or retired member of the Union Public Service Commission
10(46)	Specified income of a body, authority, board, trust or commission set up or constituted by a Central, State or Provincial Act or by Central Government or State Government, with the object of regulating or administering an activity for the benefit of the general public
10(47)	Income of Infrastructure Debt Fund
10(48)	<p>Income of a foreign company received in India in Indian currency on account of sale of crude oil or any other goods or rendering of service as notified by the Central Government, to any person in India subject to the following conditions being satisfied:</p> <p>The receipt of money is under an agreement or an arrangement which is either entered by the Central Government or approved by it</p> <p>The foreign company, and the arrangement or agreement has been notified by the Central Government having regard to the national interest in this behalf</p> <p>The receipt of the money is the only activity carried out by the foreign company in India</p>
10(48A)	<p>Any income accruing or arising to National Oil Companies and Multinational Companies on account of storage of crude oil in a facility in India and sale of crude oil therefrom to any person resident in India shall be exempt from tax, if–</p> <p>(a) such storage and sale by the foreign company is pursuant to an agreement or an arrangement entered into by the Central Government or approved by the Central Government; and</p> <p>(b) having regard to the national interest, the foreign company and the agreement or arrangement are notified by the Central Government in this behalf</p>
10(48B)	Income accruing or arising to a foreign company on account of sale of leftover stock of crude oil, if any, from the facility in India after the expiry of the agreement or arrangement
10(49)	Any income of the National Financial Holdings Company Limited
10(50)	Any income arising from specified services provided (on or after the date on which the provisions of Chapter VIII of the Finance Act, 2016 comes into force) and chargeable to equalization levy under that Chapter, shall be exempt from income-tax
10A	Income of undertakings established in Free Trade Zones, Electronic Hardware Technology Park, Software Technology Park or Special Economic Zone
10AA	Units newly established in SEZ on or after 1st April 2005, but before 1st April 2020.

Section Number	Income
10A(1A)	Exemption available under section 10A only if return of income is furnished on or before due date
10B	Income of hundred per cent export-oriented undertakings
10BA	Income from export of artistic hand-made wooden articles
11	Income from property held for charitable or religious purposes
13A	Income from house property, capital gains and income from other sources of a political party
13B	Voluntary contributions received by Electoral Trust

Notes:

1. In particular, exemptions under the following sections must be focused upon, in assessment of Individuals:

Section 10(1), 10(2), 10(2A), 10(5), 10(7), 10(10), 10(10A), 10(10AA), 10(10B), 10(10C), 10(10CC), 10(10D), 10(11), 10(12), 10(13), 10(13A), 10(14), 10(15), 10(16), 10(17), 10(17A), 10(32), 10(33), 10(34), 10(35), 10(37), 10(38), 10AA.

2. Exemption under section 10(1) has been explained in this chapter. All other exemptions available for Individuals have been discussed in later chapters, at appropriate places.

INCOME EXEMPT UNDER SECTION 10(1)**7.3**

1. Under this section, **agricultural income** of the assessee is exempt from tax.
2. According to Section 2(1A) of the Income Tax Act, 1961, 'Agricultural Income' means,
 - (a) any rent or revenue derived from *land* which is *situated in India* and used for *agricultural purposes*;
 - (b) any income derived from *such land* by agricultural operations including processing of the agricultural produce, raised or received as rent-in-kind so as to render it fit for the market, or sale of such produce; and
 - (c) income attributable to a farm house subject to the conditions that the building is situated on or in the immediate vicinity of the land and is used as a dwelling house, store house or let out-building; and the land is assessed to land revenue or a local rate or, alternatively, the building is situated on or in the immediate vicinity of land which (though not assessed to land revenue or local rate) is situated outside the urban areas i.e., any area which comprised within the jurisdiction of a municipality or cantonment board having population of ten thousand or more or in any area within such notified distance (up to eight kilometers) from the local limits of such municipality or cantonment board.
3. Income derived from saplings or seedlings grown in a nursery shall be deemed to be agricultural income.

4. Partly Agricultural Income and Partly Business Income:

- (i) Where an assessee manufactures or produces any product using agricultural produce grown or cultivated by him as raw-material, the profit on sale of such product is considered as 'partly agricultural income and partly business income'.
- (ii) Such profits are exempt to the extent they are considered as 'agricultural income' and the balance of profits are taxable as 'income from business'.
- (iii) Of the total profits from sale of such product, the difference between 'market value of agricultural produce on the date of its transfer to factory from the land' **and** 'cost of cultivation' is considered as agricultural income.
- (iv) However, where the assessee is engaged in growing and manufacturing of certain specified products, the division of 'agricultural' and 'non-agricultural' income is prescribed in the Act, which is as follows:

Assessee is engaged in	Extent to which the profit is–	
	Agricultural Income	Business Income
Growing and Manufacture of Tea	60%	40%
Growing and Manufacturing Rubber	65%	35%
Growing and Curing Coffee	75%	25%
Growing, Curing, Roasting and Grounding Coffee	60%	40%

5. Although 'agricultural income from **India**' is exempt from tax, it is considered while computing tax-liability.

PROBLEMS RELATING TO AGRICULTURAL INCOME**Illustration 1 Problem on determination of agricultural and non-agricultural income**

State whether the following are agricultural or non-agricultural incomes

- (a) Income from interest on arrears of rent payable in respect of land used for agricultural purposes
- (b) Income from agricultural land situated in Australia
- (c) Income from sale of forest trees of spontaneous growth
- (d) Income from lease of land for grazing of cattle required for agricultural pursuits
- (e) Income from interest on simple mortgage of land used for agriculture
- (f) Rent received from house property situated in a village
- (g) Remuneration received as manager of an agricultural farm house
- (h) Income from dairy farm, poultry farming, etc.,

(Bangalore University, B.Com., December 2015)

Solution:

Income	Agricultural Income/Non-agricultural Income
(a) Income from interest on arrears of rent payable in respect of land used for agricultural purposes	Non-agricultural Income
(b) Income from agricultural land situated in Australia	Non-agricultural Income
(c) Income from sale of forest trees of spontaneous growth	Non-agricultural Income
(d) Income from lease of land for grazing of cattle required for agricultural pursuits	Non-agricultural Income
(e) Income from interest on simple mortgage of land used for agriculture	Non-agricultural Income
(f) Rent received from house property situated in a village	Non-agricultural Income
(g) Remuneration received as manager of an agricultural farm house	Non-agricultural Income
(h) Income from dairy farm, poultry farming, etc.	Non-agricultural Income

Illustration 2 Problem on determination of agricultural and non-agricultural income

State whether the following are agricultural or non-agricultural incomes:

- (a) Income from agricultural land situated in Australia
- (b) Income derived from sale of seeds
- (c) Income from sale of forest trees of spontaneous growth
- (d) Lease rent received from land given to tenants for agricultural operations
- (e) Income derived from land used as stone quarries
- (f) Income from sale of plants from nursery

(Bangalore University, B.Com., December 2016)

Solution:

Income	Agricultural Income/Non-agricultural Income
Income from agricultural land situated in Australia	Non-agricultural Income
Income derived from sale of seeds	Agricultural Income
Income from sale of forest trees of spontaneous growth	Non-agricultural Income
Lease rent received from land given to tenants for agricultural operations	Agricultural Income
Income derived from land used as stone quarries	Non-agricultural Income
Income from sale of plants from nursery	Agricultural Income

FUNDAMENTAL PROBLEMS ON COMPUTATION OF TAXABLE INCOME (PROBLEMS ON INCIDENCE OF TAX)

Illustration 3 Problem on Computation of Taxable Income based on Residential Status

Following are the incomes of Mohan during previous year 2017-18:

- (a) Interest on Saving Bank Deposit in Allahabad Bank, Delhi – ₹1,200.
- (b) Income from agriculture in Africa, invested in Nepal – ₹10,000.
- (c) Dividends received in U.K. from an American Company, out of which ₹2,000 were remitted to India – ₹10,000.
- (d) Salary drawn for three months for working in Indian Embassy's Office in Australia and salary received there – ₹72,000.
- (e) Income from a building situated in Pakistan, out of which ₹10,000 was deposited in a bank in Pakistan, and the balance deposited in a Bank Account in India – ₹15,000.
- (f) Pension received in Belgium for services rendered in India with a limited company – ₹20,000.
- (g) Agricultural Income from India – ₹1,00,000.
- (h) Profits from business in UK, controlled from India – ₹2,00,000.

You are required to compute his gross total income of Mr. Mohan for the assessment year 2018-19, if he is – (i) a resident and ordinarily a resident; (ii) a resident, but not ordinarily a resident; and (iii) a non-resident.

Solution:

Statement showing computation of Gross Total Income

Income	Analysis (whether the income must be 'considered or not')	Exempt/ Taxable	Taxable Income, when Mohan is–		
			Resident and Ordinarily a Resident ₹	Resident, but not Ordinarily a Resident ₹	Non-resident ₹
Interest on Saving Bank Deposit in Allahabad Bank, Delhi.	Indian Income. Must be considered in all cases	Taxable	1,200	1,200	1,200
Income from Agriculture in Africa, invested in Nepal	Foreign Income. Must be considered only for 'Resident and Ordinarily a Resident'	Taxable	10,000	Nil	Nil

7.14 • Income Tax-I

Income	Analysis (whether the income must be 'considered or not')	Exempt/ Taxable	Taxable Income, when Mohan is–		
			Resident and Ordinarily a Resident ₹	Resident, but not Ordinarily a Resident ₹	Non-resident ₹
Dividends received in UK from an American Company, out of which ₹2,000 was remitted to India.	Foreign Income. Amount remitted to India does not represent 'received in India'. Must be considered only for 'Resident and Ordinarily a Resident'	Taxable	10,000	Nil	Nil
Salary drawn for three months for working in Indian Embassy's Office in Australia and salary received there – ₹72,000.	Indian Income, being Income deemed to accrue in India. Must be considered in all cases	Taxable	72,000	72,000	72,000
Income from a building situated in Pakistan, out of which ₹10,000 was deposited in a bank in Pakistan, and the balance deposited in a Bank Account in India – ₹15,000.	₹5,000 is Indian Income (on receipt basis) – It must be considered in all cases. Remaining ₹10,000 is Foreign Income – It must be considered only for 'Resident and Ordinarily a Resident'	Taxable	15,000	5,000	5,000
Pension received in Belgium for services rendered in India with a limited company – ₹20,000.	Indian Income, being accrued in India. Must be considered in all cases	Taxable	20,000	20,000	20,000
Agricultural Income from India – ₹1,00,000.	Indian Income. Must be considered in all cases	Exempt u/s 10(1)	Exempt	Exempt	Exempt
Profits from business in UK, controlled from India ₹2,00,000.	Foreign Income. Must be considered only for 'Resident'	Taxable	2,00,000	2,00,000	Nil
Gross Total Income			3,28,200	2,98,200	98,200

Notes:

1. Students can present only Income and Amount Columns in examinations. The Analysis and Taxability columns can be avoided.
2. All further problems and solutions are shown without Analysis and Taxability Columns.

Illustration 4 Problem on Computation of Taxable Income based on Residential Status

Mr. Anand receives the following incomes:

- (a) Salary ₹24,000 from an Indian Company.
- (b) Dividend from a foreign company received in London ₹30,000.
- (c) Share of profit received in London from a business situated in Sri Lanka but controlled from India ₹60,000.
- (d) Dividend received in Germany from an Indian Company ₹28,000.

Compute gross total income of Anand, if he is: (a) Resident and Ordinarily Resident (b) Resident but Not Ordinarily Resident & (c) Non-Resident.

Solution:

Statement showing computation of Gross Total Income

Particulars of Income	Nature of Income	When Mr. Anand is–		
		Ordinarily Resident ₹	Not ordinarily Resident ₹	Non-Resident ₹
Salary from an Indian Company	Indian Income	24,000	24,000	24,000
Dividend from a foreign company received in London	Foreign Income	30,000	–	–
Share of profit received in London from a business situated in Sri Lanka but controlled from India	Foreign Income-business controlled from India	60,000	60,000	–
Dividend received in Germany from an Indian Company	Indian Income	Exempt u/s 10(34)	Exempt u/s 10(34)	Exempt u/s 10(34)
Gross Total Income		1,14,000	84,000	24,000

Illustration 5 Problem on Computation of Taxable Income based on Residential Status

Ms. Bharathi furnishes the following particulars of her income:

- (a) Royalty earned in India but received in Nepal ₹46,000
- (b) Dividend from a foreign company received in Nepal ₹56,000
- (c) Share of profit from a business situated in Nepal received in Burma but business is controlled from India ₹42,000
- (d) Rent of house property situated in Nepal and received there ₹1,65,000
- (e) Speculation profit earned and received in America ₹60,000

Compute gross total income of Ms. Bharathi, if she is: (a) Resident and Ordinarily Resident (b) Resident but Not Ordinarily Resident & (c) Non-Resident.

Solution:**Statement showing Gross Total Income**

Particulars of Income	Nature of Income	When Ms. Bharathi is–		
		Ordinarily Resident ₹	Not ordinarily Resident ₹	Non-Resident ₹
(a) Royalty earned in India but received in Nepal	Indian Income	46,000	46,000	46,000
(b) Dividend from a foreign company received in Nepal	Foreign Income	56,000	–	–
(c) Share of profit from a business situated in Nepal received in Burma but business is controlled from India	Foreign Income-business controlled from India	42,000	42,000	–
(d) Rent of house property situated in Nepal and received there	Foreign Income	1,65,000	–	–
(e) Speculation profit earned and received in America	Foreign Income	60,000	–	–
Gross Total Income		3,69,000	88,000	46,000

Illustration 6 Problem on Computation of Taxable Income based on Residential Status

Mr. Chandru furnishes the following particulars of his income:

- Interest on German Development Bonds (2/5th received in India) ₹60,000
- Income from agriculture in Bangladesh (received there but later on ₹50,000 remitted to India) ₹1,81,000
- Income from property in Canada received there (₹76,000 is used in Canada for meeting the educational expenses of Chandru's son in USA and ₹10,000 is later on remitted to India) ₹86,000
- Income from business in Kenya which is controlled from Bangalore (₹15,000 is received in Bangalore) ₹65,000
- Dividend paid by an Indian Company but received in Canada ₹46,500
- Past untaxed profit of ₹10,50,000 brought to India during the current previous year
- Profit from business in Mysore but managed from London ₹27,000
- Profit on sale of building in Mangalore but received in Sri Lanka ₹4,80,000
- Pension from a former employer in India received in Rangoon ₹36,000
- Gift in foreign currency from a friend received in India ₹80,000

Compute gross total income of Ms. Chandru, if he is:

- Resident and Ordinarily Resident
- Resident but Not Ordinarily Resident, and
- Non-Resident.

Solution:**Statement showing computation of Gross Total Income**

Particulars of Income	Nature of Income	When Mr. Chandru is–		
		Ordinarily Resident ₹	Not ordinarily Resident ₹	Non-Resident ₹
(a) <u>Interest on German Development Bonds</u>				
• Received in India ($60,000 \times 2/5$)	Indian Income	24,000	24,000	24,000
• Received outside India ($60,000 \times 3/5$)	Foreign Income	36,000	–	–
(b) Income from agriculture in Bangladesh	Foreign Income	1,81,000	–	–
(c) Income from property in Canada received there	Foreign Income	86,000	–	–
(d) <u>Income from business in Kenya which is controlled from Bangalore</u>				
• Received in India	Indian Income	15,000	15,000	15,000
• Received outside India	Foreign Income-business controlled from India	50,000	50,000	–
(e) Dividend paid by an Indian Company but received in Canada	Indian Income	Exempt	Exempt	Exempt
(f) Past untaxed profit brought to India during the relevant previous year	Not an income at all	–	–	–
(g) Profit from business in Mysore but managed from London	Indian Income	27,000	27,000	27,000
(h) Profit on sale of building in Mangalore but received in Sri Lanka	Indian Income	4,80,000	4,80,000	4,80,000
(i) Pension from a former employer in India received in Rangoon	Indian Income	36,000	36,000	36,000
(j) Gift in foreign currency from a friend received in India	Indian Income	80,000	80,000	80,000
Gross Total Income		10,15,000	7,12,000	6,62,000

Note: 'Gift from a friend' is considered as 'income' for tax purposes; and it is a taxable income.

Illustration 7 Problem on Computation of Taxable Income based on Residential Status

Mr. Dhananjay receives the following incomes:

- (a) Profit on sale of plant at London ₹1,50,000 (50% is received in India)
- (b) Profit on sale of plant at Delhi ₹1,00,000 (50% is received in London)
- (c) Salary from an Indian Company received in London ₹60,000 (50% is paid for rendering services in India)
- (d) Interest on UK Development Bonds ₹40,000 (entire amount is received in London)
- (e) Income from property in London received there ₹30,000
- (f) Income from agriculture in London received there, 50% of which is used for meeting the hostel expenses of Mr. Dhananjay's daughter in England and remaining amount is later on remitted to India ₹50,000
- (g) Dividend received in London from a company registered in India but mainly operating from UK ₹17,000
- (h) Profit from a business in Delhi ₹50,000
- (i) Rental income from a property in Nepal deposited by the tenant in a foreign branch of an Indian Bank operating there ₹1,20,000

Compute gross total income of Mr. Dhananjay, if he is: (a) Resident and Ordinarily Resident (b) Resident but Not Ordinarily Resident, and (c) Non-Resident.

Solution:

Statement showing computation of Gross Total Income

Particulars of Income	Nature of Income	When Mr. Dhananjay is—		
		Ordinarily Resident ₹	Not ordinarily Resident ₹	Non-Resident ₹
(a) Profit on sale of plant at London				
• Received in India ($1,50,000 \times \frac{1}{2}$)	Indian Income	75,000	75,000	75,000
• Received outside India ($1,50,000 \times \frac{1}{2}$)	Foreign Income	75,000	—	—
(b) Profit on sale of plant at Delhi	Indian Income	1,00,000	1,00,000	1,00,000
(c) Salary from Indian Company received in London	Indian Income	60,000	60,000	60,000
(d) Interest on UK Development Bonds received in London	Foreign Income	40,000	—	—
(e) Income from property in London received there	Foreign Income	30,000	—	—
(f) Income from agriculture in London received there	Foreign Income	50,000	—	—

Particulars of Income	Nature of Income	When Mr. Dhananjay is–		
		Ordinarily Resident ₹	Not ordinarily Resident ₹	Non-Resident ₹
(g) Dividend received in London from a company registered in India but mainly operating from UK	Indian Income	Exempt	Exempt	Exempt
(h) Profit from a business in Delhi	Indian Income	50,000	50,000	50,000
(i) Rental income from a property in Nepal deposited by the tenant in a foreign branch of an Indian Bank operating there	Foreign Income	1,20,000	–	–
Gross Total Income		6,00,000	2,85,000	2,85,000

Illustration 8 Problem on Computation of Taxable Income based on Residential Status

Mr. Nagaraju furnishes the following details of his income:

- Royalty income received from the Government Company ₹42,000
- Income from business earned in Afghanistan ₹52,000 of which ₹25,000 is received in India. (Business is controlled from Bangalore)
- Interest received from Mr. Manjunath a non-resident against a loan provided to him to run a business in India ₹50,000
- Royalty received from Mr. Kumar a resident for technical services provided to run a business outside India ₹20,000
- Income from business in Jaipur ₹40,000. Business is controlled from France and ₹8,000 is remitted to France
- Share of profit from HUF ₹2,00,000
- Dividends from UK based company – ₹27,000

Compute gross total income when Mr. Nagaraju is: (a) Resident and Ordinarily Resident (b) Resident but Not Ordinarily Resident & (c) Non-Resident.

Solution:

Statement showing computation of Gross Total Income

Particulars of Income	Nature of Income	When Mr. Nagaraju is–		
		Ordinarily Resident ₹	Not ordinarily Resident ₹	Non-Resident ₹
(a) Royalty income received from the Government Company	Indian Income	42,000	42,000	42,000

7.20 • Income Tax - I

Particulars of Income	Nature of Income	When Mr. Nagaraju is–		
		Ordinarily Resident ₹	Not ordinarily Resident ₹	Non-Resident ₹
(b) <u>Income from business earned in Afghanistan</u>				
• Received in India 25,000	Indian Income	25,000	25,000	25,000
• Received outside India 27,000	Foreign Income–Business controlled from India	27,000	27,000	–
(c) Interest received from Mr. Manjunath a non-resident against a loan provided to him to run a business in India	Indian Income	50,000	50,000	50,000
(d) Royalty received from Mr. Kumar a resident for technical services provided to run a business outside India	Indian Income	20,000	20,000	20,000
(e) Income from business in Jaipur	Indian Income	40,000	40,000	40,000
(f) Share of profit from HUF (Exempt u/s 10(2))	Indian Income	Exempt	Exempt	Exempt
(g) Dividends from UK based company	Foreign Income	27,000	–	–
Gross Total Income		2,31,000	2,04,000	1,77,000

Notes:

1. Interest on loan given for a 'business in India' is Indian Income.
2. Royalty received from a 'resident' is Indian income irrespective of whether the service is utilized in India or outside India.

Illustration 9 Problem on Computation of Taxable Income based on Residential Status

Mr. Gautam furnishes the following particulars of his income earned during the Previous year 2017-18:

- (a) Interest on Singapore Development Bonds ₹1,50,000 (1/3 received in India)
- (b) Income from agriculture in Sri Lanka remitted to India ₹1,90,000
- (c) Income from property in Mexico received there ₹2,22,000
- (d) Income from business in Kuwait controlled from Mumbai ₹85,000 (₹35,000 received in India)
- (e) Dividend from an Indian Company received in Nepal ₹44,000
- (f) Royalty received in Singapore from Mr. Rajesh, a resident in India for technical services provided to him in connection with his business there ₹33,000

- (g) Profit from business in Chennai. The business is controlled from Singapore ₹2,25,000
 (h) Profit on sale of building in Bangalore received in Nepal ₹5,20,000
 (i) Income from agriculture in Punjab received in London ₹1,40,000
 (j) Profit from business in Indonesia ₹1,60,000 (The business is controlled from Bangalore and 60% of the profit is deposited there and 40% is remitted to India)
 (k) Interest received from Mr. Prakash a non-resident on loan provided to him to pursue education in USA ₹1,50,000

Compute gross total income when Mr. Gautam is: (a) Resident and Ordinarily Resident (b) Resident but not Ordinarily a Resident & (c) Non-Resident.

Solution:

Statement showing computation of Gross Total Income

Particulars of Income	Nature of Income	When Mr. Gautam is–		
		Ordinarily Resident ₹	Not ordinarily Resident ₹	Non-Resident ₹
(a) <u>Interest on Singapore Development Bonds</u>				
• Received in India (1,50,000 × 1/3)	Indian Income	50,000	50,000	50,000
• Received outside India (1,50,000 × 2/3)	Foreign Income	1,00,000	–	–
(b) Income from agriculture in Sri Lanka	Foreign Income	1,90,000	–	–
(c) Income from property in Mexico received there	Foreign Income	2,22,000	–	–
(d) <u>Income from business in Kuwait controlled from Mumbai</u>				
• Received in India 35,000	Indian Income	35,000	35,000	35,000
• Received outside India 50,000	Foreign Income– Business controlled from India	50,000	50,000	–
(e) Dividend from an Indian Company	Indian Income	Exempt	Exempt	Exempt
(f) Royalty received in Singapore	Foreign Income	33,000	–	–
(g) Profit from business in Chennai	Indian Income	2,25,000	2,25,000	2,25,000
(h) Profit on sale of building in Bangalore	Indian Income	5,20,000	5,20,000	5,20,000
(i) Income from agriculture in Punjab	Indian Income	Exempt	Exempt	Exempt
(j) Profit from business in Indonesia	Foreign Income– Business controlled from India	1,60,000	1,60,000	–

Particulars of Income	Nature of Income	When Mr. Gautam is–		
		Ordinarily Resident ₹	Not ordinarily Resident ₹	Non-Resident ₹
(k) Interest received from Mr. Prakash (assumed to be received in India)	Indian Income	1,50,000	1,50,000	1,50,000
Gross Total Income		17,35,000	11,90,000	9,80,000

Illustration 10 Problem on Computation of Taxable Income based on Residential Status

Mr. Harish furnishes the following details of his income:

- Income from business in Kolkata managed in USA ₹25,000
- Income from pension for services rendered in India received in London ₹15,000
- Income from property in Burma received in India ₹10,000
- Profit from business in Sri Lanka deposited in bank there ₹15,000
- Income from profession in Kenya received there but the profession was set up in India ₹15,000
- Income on UK Government Securities ₹50,000 (1/2 received in India)
- Income from agriculture in America received there but later on remitted to India ₹80,000
- Income from agriculture in India received in America ₹1,25,000
- Income from property in Canada received there ₹40,000
- Income from business in Uganda, which is controlled from Bangalore ₹45,000 (₹25,000 is received in India)
- Profit on sale of building in Mysore but received in Sri Lanka ₹1,80,000
- Salary received in India for services rendered in California ₹80,000
- Income earned and received in Switzerland from fixed deposits ₹1,30,000
- Income from business in Bhopal received in Singapore ₹60,000
- Interest accrued but not received on Fixed Deposits in a Bank in Texas ₹45,000
- Income from agriculture in England, all spent for the education of children studying there ₹48,000

Show the incomes that are to be considered in the computation of gross total income and calculate gross total income when Mr. Harish is:

- Resident and Ordinarily Resident
- Resident but Not Ordinarily Resident, and
- Non-Resident.

Solution:**Statement showing computation of Gross Total Income**

Particulars of Income	Nature of Income	When Mr. Harish is–		
		Ordinarily Resident ₹	Not ordinarily Resident ₹	Non-Resident ₹
(a) Income from business in Kolkata managed in USA	Indian Income	25,000	25,000	25,000
(b) Income from pension for services rendered in India received in London	Indian Income	15,000	15,000	15,000
(c) Income from property in Burma received in India	Indian Income	10,000	10,000	10,000
(d) Profit from business in Sri Lanka deposited in bank there	Foreign Income	15,000	–	–
(e) Income from profession in Kenya received there but the profession was set up in India	Foreign Income–Profession controlled from India	15,000	15,000	–
(f) <u>Income on UK Government Securities</u>				
• Received in India ($50,000 \times \frac{1}{2}$)	Indian Income	25,000	25,000	25,000
• Received outside India ($50,000 \times \frac{1}{2}$)	Foreign Income	25,000	–	–
(g) Income from agriculture in America received there but later on remitted to India	Foreign Income	80,000	–	–
(h) Income from agriculture in India received in America	Indian Income	Exempt	Exempt	Exempt
(i) Income from property in Canada received there	Foreign Income	40,000	–	–
(j) <u>Income from business in Uganda, which is controlled from Bangalore</u>				
• Received in India	Indian Income	25,000	25,000	25,000
• Received outside India	Foreign Income–Business controlled from India	20,000	20,000	–
(k) Profit on sale of building in Mysore but received in Sri Lanka	Indian Income	1,80,000	1,80,000	1,80,000

7.24 • Income Tax - I

Particulars of Income	Nature of Income	When Mr. Harish is–		
		Ordinarily Resident ₹	Not ordinarily Resident ₹	Non-Resident ₹
(l) Salary received in India for services rendered in California	Indian Income	80,000	80,000	80,000
(m) Income earned and received in Switzerland from fixed deposits	Foreign Income	1,30,000	–	–
(n) Income from business in Bhopal received in Singapore	Indian Income	60,000	60,000	60,000
(o) Interest accrued but not received on Fixed Deposits in a Bank in Texas	Foreign Income	45,000	–	–
(p) Income from agriculture in England, all spent for the education of children studying there	Foreign Income	48,000	–	–
Gross Total Income		8,38,000	4,55,000	4,20,000

Illustration 11 Problem on determination of residential status and computation of taxable income

Ms. Indira is a foreign citizen and visited India for the first time during the Previous Year 2013-14 and stayed for 180 days. During the subsequent Previous Years her stay was as follows: 2014-15 – 58 days; 2015-16 – 180 days; 2016-17 – 58 days and 2017-18 – 180 days.

Determine the residential status of Ms. Indira for the Assessment Year 2018-19 and show the amount to be considered in the computation of gross total income for the Assessment Year 2018-19.

- (a) Consultation fee received from Indian Company ₹65,000
- (b) Profit from business in America ₹75,000 (₹25,000 received in India)
- (c) Profit from business in England ₹90,000 (Business controlled from Bengaluru)
- (d) Income from agricultural operations in America ₹50,000
- (e) Income from agricultural operations in Mandya ₹80,000

Solution:
Step 1: Determination of Residential Status
Ascertainment of Number of Days of Stay in India during different previous years

YEAR	Total No. of Days of Stay
2017-2018	180
2016-2017	58

YEAR	Total No. of Days of Stay
2015-2016	180
2014-2015	58
2013-2014	180

Verification of Fulfillment of Conditions Under Section 6(1)

Condition Under Section 6(1)	Fulfilled or Not Fulfilled
(a) The Individual must be in India for at least 182 days during the relevant previous year (i.e., 2017-18)	Not Fulfilled
(b) The Individual must be in India for at least 60 days during the relevant previous year (i.e., 2017-18) and at least 365 days during four previous years immediately preceding the relevant previous year (i.e., 2017-18)	Fulfilled Fulfilled

Since Indira has fulfilled one of the conditions under section 6(1), she is a **resident in India** for Assessment Year 2018-19.

Note:

Indira is a foreign citizen. Hence, in the condition under section 6(1)(b), 60 days have been considered.

Verification of Fulfillment of Conditions under Section 6(6)

Condition Under Section 6(6)	Fulfilled or Not Fulfilled
(i) The Individual must be resident in India for at least 2 out of 10 previous years immediately preceding the relevant previous year (i.e., 2017-18)	Fulfilled
(ii) The Individual must be in India for at least 730 days during 7 previous years immediately preceding the relevant previous year (i.e., 2017-18)	Not Fulfilled

Since Indira, a resident individual, has fulfilled only one of the conditions under section 6(6), she is a '**resident, but not ordinarily a resident**'.

Step 2: Ascertainment of Incidence of Tax**Computation of Gross Total Income**

	Type of Income	₹
Consultation fee received from Indian company	Indian income	65,000
Profit from business in America		
• Received in India	Indian income	25,000
• Received outside India	Foreign income	—
Profit from business in England, controlled from India	Foreign income	90,000
Agricultural income in USA	Foreign income	—
Agricultural income in India	Indian income	Exempt u/s 10(1)
Gross Total Income		1,80,000

SUMMARY

- On classifying the 'incomes that must be considered' into revenue receipts and capital receipts, the next step is to identify incomes which are taxable.
- The taxability of an income can be identified with the help of the golden rule of income tax.
- The Golden Rule of Income Tax states that "All Revenue Receipts are Taxable, unless specifically Exempt, **and** All Capital Receipts are Exempt, unless specifically Taxable.
- Revenue incomes exempt from tax is given under Section 10 of the Income Tax Act.
- Exemptions under the following sections must be focused upon, in assessment of Individuals:
- Sections 10(1), 10(2), 10(2A), 10(5), 10(7), 10(10), 10(10A), 10(10AA), 10(10B), 10(10C), 10(10CC), 10(10D), 10(11), 10(12), 10(13), 10(13A), 10(14), 10(15), 10(16), 10(17), 10(17A), 10(32), 10(33), 10(34), 10(35), 10(37), 10(38), 10AA.
- Sections 10(1) provides exemption for Agricultural Income.
- Agricultural income refers to income derived from cultivation and related activities from a land situated in India.
- Where an assessee is using any agricultural produce cultivated by him/her in manufacturing any product, the profit on sale of such product is considered as 'partly agricultural income and partly business income'.

THEORY QUESTIONS**Section A Type Questions**

1. State the Golden Rule of Income Tax.
2. List any five incomes exempt from tax.
3. Define Agricultural Income. (Bangalore University, B.Com., Nov/Dec 2015)
4. What do you mean by Agricultural Income? (Bangalore University, B.Com., Nov/Dec 2016)
5. Give any two examples of agricultural income. (Bangalore University, B.Com., Nov/Dec 2014)
6. What is 'partly agricultural income'?

7. How is 'partly agricultural income' (other than in case of specified businesses) disintegrated into agricultural and business income?
8. What is the exemption under section 10A for?
9. What is the income exempt under section 10AA?

Section B Type Questions

1. List any twelve incomes exempt in case of individual assesseees.
2. What is 'agricultural income'?
3. Explain the meaning of 'partly agricultural income' and its tax-treatment.
4. Explain briefly the exemption under section 10A.
5. Explain the exemption under section 10AA, in brief.

EXERCISES

Section B

1. Following are the taxable incomes of Mr. Sharath Kumar
 - (a) Profit of a hotel business in Sydney ₹2,00,000
 - (b) Dividend declared in Paris but received in India ₹1,10,000
 - (c) Dividend from a domestic company ₹25,000
 - (d) Income accrued in Bengaluru but received in Singapore ₹60,000
 - (e) Past untaxed income brought to India ₹50,000

Compute the Total Taxable Income for the AY 2018-19 if the assessee is (a) Resident (b) Not ordinarily Resident and (c) Non-resident

(Bangalore University, BBM, Nov/Dec 2014)

(Ans: (a) ₹3,70,000, (b) ₹1,70,000 and (c) ₹1,70,000)

[Hint:

- (i) Unless specifically mentioned, income is assumed to be received in the place of accrual. Hence, Profits from hotel business in Sydney is considered as received in Sydney and therefore is considered only when the assessee is a Resident and Ordinarily a Resident
- (ii) Dividends from domestic company is exempt from tax
- (iii) Past untaxed income brought into India is not taxable]

Section C

1. From the following particulars of Mr. Naveen, compute his Gross Total Income for the AY 2018-19 if he is (a) Ordinary Resident (b) Not Ordinary Resident and (c) Non Resident
 - (a) Income from business in Chennai, business managed from Sri Lanka ₹25,000
 - (b) Income from house property in Mysuru ₹1,00,000
 - (c) Income from salary in Japan ₹1,60,000
 - (d) Income from business in Kuwait, business being controlled from Mumbai ₹65,000. (₹25,000 is received in India)
 - (e) Income from agriculture in Punjab received in Mumbai ₹30,000

7.28 • Income Tax - I

- (f) Income from agriculture in Bangladesh remitted to India ₹10,000
- (g) Profit from sale of building in India ₹2,50,000
- (h) Profit from business in Indonesia ₹40,000. This business is controlled from Delhi
- (i) Income from Indian Partnership Firm ₹5,000
- (j) Interest on Savings Bank Deposits in State Bank of India ₹1,000
- (k) Dividend from Foreign Company received in England ₹10,000
- (l) Interest on German Development Bonds ₹51,000 (1/3 received in India)

(Bangalore University, B.Com, Oct/Nov 2012)

(Ans: (a) ₹7,12,000, (b) ₹4,98,000, and (c) ₹4,18,000)

[Hint:

- (i) Income from business outside India but controlled from India is taxable only in the hands of Ordinarily Resident and Not-ordinarily Resident.
 - (ii) Agricultural Income in India and Income from Partnership Firm are exempt from tax.
 - (iii) Remittance to India is not 'receipt in India'. Hence, Income from agriculture in Bangladesh is foreign income.]
2. From the following particulars of Mr. Naveen, compute his Gross Total Income for the AY 2018-19, if he is (a) Ordinary Resident (b) Not Ordinary Resident, and (c) Non Resident
- (a) Profit from business in England received in India ₹24,000
 - (b) Income from house property in Pakistan received there ₹20,000
 - (c) Profit from business in Iran received in India ₹10,000
 - (d) Income from house property in Bangladesh deposited in a bank there ₹10,000
 - (e) Profit from business in Indonesia deposited in a bank there. This business is controlled from India ₹30,000
 - (f) Profit from software business in Bengaluru controlled from USA ₹30,000
 - (g) Income from agriculture in Punjab ₹20,000
 - (h) Profit from sale of building in India received in Sri Lanka ₹25,000
 - (i) Income accrued in Chennai but received in Singapore ₹32,000
 - (j) Dividend received from Domestic Company ₹10,000

(Bangalore University, B.Com, Nov/Dec 2013)

(Ans: (a) ₹1,81,000, (b) ₹1,51,000 and (c) ₹1,21,000)

[Hint:

- (i) Agriculture Income from India and Dividend from Domestic Companies are exempt from tax.
 - (ii) Income from business outside India but controlled from India is taxable only in the hands of Ordinarily Resident and Not-ordinarily Resident.]
3. Mr. Nischay furnishes the following particulars of his income earned during the PY 2017-18
- (a) Profit from business in Chennai ₹50,000
 - (b) Income from agriculture in Sri Lanka ₹1,90,000
 - (c) Income from property in Mexico received there ₹2,00,000
 - (d) Interest on Singapore Development Bonds ₹1,50,000 (1/3 received in India)
 - (e) Income from business in Kuwait controlled from Mumbai ₹85,000 (₹35,000 received in India)

- (f) Dividend from domestic company ₹1,000
- (g) Profit on sale of building in Bengaluru received in Nepal ₹50,000
- (h) Income from agriculture in Punjab ₹1,00,000
- (i) Profit on sale of plant at London ₹50,000 (50% is received in India)
- (j) Income from house property in Nepal received there ₹20,000
- (k) Profit from business in Mysuru received in Mandya ₹25,000
- (l) Dividends from UK based company received in UK ₹27,000

Compute his Gross Total Income for the AY 2018-19 if he is (a) Ordinary Resident (b) Not Ordinary Resident, and (c) Non Resident

(Bangalore University, B.Com, Nov/Dec 2014)

(Ans: (a) ₹8,47,000 (b) ₹2,85,000, and (c) ₹2,35,000)

[Hint:

- (i) Agriculture Income from India and Dividend from Domestic Companies are exempt from tax.
 - (ii) Income from business outside India but controlled from India is taxable only in the hands of Ordinarily Resident and Not-ordinarily Resident.]
4. Following are the incomes of Mr. Vishnu for the PY 2017-18
- (a) Received ₹20,000 in India, which accrued in England
 - (b) ₹10,000 earned in India but received in England
 - (c) ₹5,000 were earned and received in Africa but brought to India
 - (d) ₹10,000 were earned and received in Japan from a business which was controlled and managed in Japan
 - (e) ₹16,000 was untaxed foreign income of some earlier year, which was brought to India in the PY
 - (f) Interest on fixed deposit in SBI, Bengaluru ₹1,200
 - (g) Income from agriculture in Africa ₹10,000
 - (h) Dividends received in UK from an American Company ₹10,000
 - (i) Salary income for three months for working in Indian Embassy's office in Australia and salary received there ₹72,000
 - (j) Income from house property in Mumbai ₹1,00,000
 - (k) Interest received on Post Office Savings Bank A/c ₹1,000
 - (l) Pension income from Belgium for services rendered in India with a limited company ₹20,000
 - (m) Gift from relatives ₹80,000

Which of the above incomes are taxable if Mr. Vishnu is (a) Resident and Ordinarily Resident (b) Resident but not Ordinarily Resident, and (c) Non-Resident

(Bangalore University, B.Com, Nov/Dec 2015)

(Ans: (a) ₹2,58,200 (b) ₹2,23,200, and (c) ₹2,23,200)

[Hint:

- (i) Unless specifically mentioned, income is assumed to be received in the place of accrual.
- (ii) Past untaxed income brought into India is not taxable.

- (iii) Salary income for working in Indian Embassy's Office outside India is 'deemed to accrue in India' and hence is taxable in the hands of the assessee irrespective of the residential status.
- (iv) Interest on Post Office Savings Bank Account is exempt from tax u/s 10(15)
- (v) Gift from relatives is exempt from tax u/s 56(2).]

5. Mr. Akshay furnishes the following particulars of his income for the PY 2017-18.

- (a) Income from business in Hubballi ₹1,00,000
- (b) Profit from business in UK controlled from India ₹60,000
- (c) Income from house property in Japan received there ₹50,000
- (d) Income from business in India received in Pakistan ₹30,000
- (e) Salary received in India for services rendered in USA ₹70,000
- (f) Interest on deposits with SBI in Mysuru ₹20,000
- (g) Profit from business in Singapore controlled from India (1/3 received in India) ₹30,000
- (h) Past untaxed income brought to India ₹8,000
- (i) Dividend received from a domestic company ₹5,000
- (j) Agricultural income earned in Nepal ₹25,000
- (k) Commission received in India for service given in Japan ₹10,000
- (l) Income from profession in India but received in France ₹10,000

Determine his gross total income for the AY 2018-19, if his residential status is (a) Ordinarily Resident (b) Not Ordinarily Resident, and (c) Non Resident

(Bangalore University, B.Com, Nov/Dec 2016)

(Ans: (a) ₹4,05,000 (b) ₹3,30,000, and (c) ₹2,50,000)

[Hint:

- (i) Income from business outside India but controlled from India is taxable only in the hands of Ordinarily Resident and Not-ordinarily Resident.
- (ii) Past untaxed income brought into India is not taxable.
- (iii) Dividends from domestic company is exempt from tax.]

6. Mr. Krishna furnishes the following particulars of his income earned during the Previous Year 2017-18

- (a) Profit from business in Chennai ₹50,000
- (b) Income from agriculture in Sri Lanka ₹1,90,000
- (c) Income from property in Mexico received there ₹2,00,000
- (d) Interest on Singapore Development Bonds ₹1,50,000 (1/3 received in India)
- (e) Income from business in Kuwait controlled from Mumbai ₹85,000 (₹35,000 was received in India)
- (f) Dividend from domestic company ₹1,000
- (g) Profit on sale of building in Bengaluru received in Nepal ₹50,000
- (h) Income from agriculture in Punjab ₹1,00,000
- (i) Profit on sale of plant at London ₹50,000 (50% is received in India)
- (j) Income from house property in Nepal received in Mandya ₹25,000
- (k) Dividends from UK based company received in UK ₹27,000

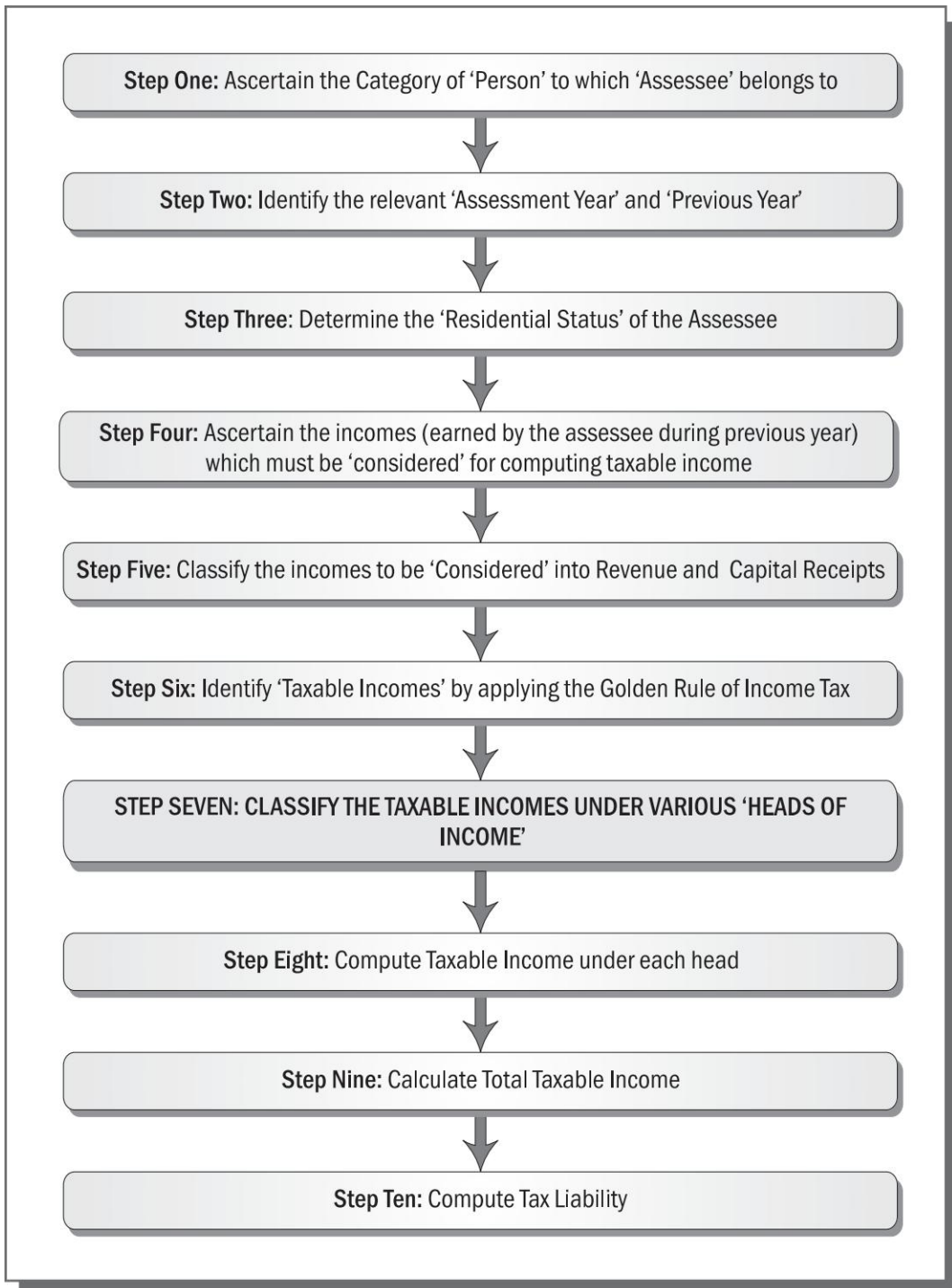
Compute his Gross Total Income for the AY 2018-19, if he is (a) Ordinarily Resident (b) Not-ordinarily Resident and (c) Non Resident

(Bangalore University, B.Com, Nov/Dec 2017)

(Ans: (a) ₹ 8,27,000 (b) ₹ 2,85,000, and (c) ₹ 2,35,000)

[Hint:

- (i) Agriculture Income from India and Dividend from Domestic Companies are exempt from tax.
- (ii) Income from business outside India but controlled from India is taxable only in the hands of Ordinarily Resident and Not-ordinarily Resident.]



Heads of Income

CHAPTER OVERVIEW

- 8.1 Introduction
- 8.2 Chargeability under the head "Income from Salaries"
- 8.3 Chargeability under the head "Income from House Property"
- 8.4 Chargeability under the head "Income from Business or Profession"
- 8.5 Chargeability under the head "Capital Gains"
- 8.6 Chargeability under the head "Income from Other Sources"

1. Income from Salaries
2. Income from House Property
3. Income from Business or Profession
4. Capital Gains
5. Income from Other Sources

An income taxable in the hands of the assessee must be charged under one of the above heads of income. The '**chargeability**' of income under a particular head depends on the fulfillment of conditions under that head.

The following paragraphs explain the conditions to be fulfilled by an income for its '**chargeability**' under a specified head of income:

On identification of incomes taxable in the hands of the assessee, the **next step** in making assessment is to classify the taxable incomes under various Heads of Income. This chapter explains the procedure for classifying taxable incomes under various heads of income.

8.1

INTRODUCTION

According to Section 14 of the Income Tax Act, 1961, taxable income of a person must be computed under the following five heads:

CHARGEABILITY UNDER THE HEAD “INCOME FROM SALARIES”

8.2

According to section 15 of the Income Tax Act, an income is chargeable under the head “Salaries” when—

- (a) The relationship between ‘payer’ and ‘assessee’ is in the nature of ‘employer-employee’; and
- (b) The payment made by ‘employer’ to assessee is ‘out of employment’.

Notes:

1. An ‘employer-employee’ relationship is bound by ‘service agreement’.
2. A contractual relationship is not ‘employer-employee’ relationship. For example, relationship between a Chartered Accountant and Client, Doctor and Patient, Lawyer and Client, etc., is governed by ‘contract’ (whether expressed or implied), and not by ‘service agreement’.
3. Once governed by ‘service agreement’, ‘employer-employee’ relationship comes into existence, irrespective of the qualification and other traits of the employee. A person may be a Medical Practitioner (Doctor) by qualification. However, once he is employed in a Medical Institution (Hospital etc.), he becomes an ‘employee’ and the payment by the Hospital to him for services rendered must be considered as ‘income from salary’ and not as ‘income from profession’.
4. Only payments made by ‘employer’ to ‘employee’ based on ‘employment’ can be considered as ‘income from salary’. For example, suppose an employee of Reliance Industries Ltd. has invested in debentures of the company. The interest on debentures paid by the company each year is not ‘income from salary’ to the assessee, although he is employee of the company, since the payment is not ‘out of employment’ (i.e., it is not based on his employment in the company). The same is the treatment even when the debentures are allotted by the company.
5. Any income arising ‘out of employment’, but not from ‘employer’ is not ‘income from salary’. For example, suppose a Professor of Commerce has been chosen by Bangalore University for setting question paper, and the selection is based on long service rendered in his college, which is affiliated to the said university. The remuneration for setting paper is not ‘income from salary’ though it is ‘out of employment’ (i.e., based on his employment) since the payment of remuneration is not by his ‘employer’.
6. Unless both the conditions specified under section 15 are fulfilled, an income cannot be charged under the head “Salaries”.

CHARGEABILITY UNDER THE HEAD “INCOME FROM HOUSE PROPERTY”

8.3

According to Section 22 of the Income Tax Act, 1961, an income is chargeable under the head ‘Income from House Property’ when the income is from a ‘property’ which can be considered under the head ‘house property’.

A 'Property' can be considered under the head 'House Property' when the following conditions are fulfilled:

- (a) The property should consist of any buildings or land appurtenant thereto;
- (b) The assessee should be the owner of the property;
- (c) The property should not be used by the owner for the purpose of any business or profession carried on by him, the profits of which are chargeable to income-tax.

Notes:

1. In this case, the conditions are applicable for the 'property' and not the 'income'.
2. The first condition for considering a 'property' under "House Property" is that the property must not be some property (like car, jewelry, etc.,) but must be a 'house property'. Under the Income Tax Act, 'House Property' means 'property consisting of buildings or land appurtenant thereto'.
3. 'Building' means 'enclosure of walls – with or without a roof'. Accordingly, a residential house, a commercial complex, an office building, a godown, swimming pool, stadium, lecture halls, convention centers etc., are buildings.
4. 'Land appurtenant' to the building means the land which is an indivisible part of the building for its use and enjoyment by the occupiers; and the land is not put to any other use and is not yielding any income assessable under the head other than "income from house property". It includes approach roads to and from the building, parking space, garden, kitchen garden, corridors, cattle-shed, space between compound wall and the main building, etc.
5. Only when a property consists of 'building and land appurtenant thereto', it can be considered as 'House Property'. So, income from letting vacant land is not 'income from house property' since there is no building. A House boat is not a 'House Property' since it is not a 'building'.
6. The second condition for considering a 'property' under the head 'house property' is that the property must be owned by the assessee. The ownership may be legal ownership or true ownership.
7. According to Section 27 of the Income Tax Act, 1961, the following are the situations where the assessee is not the 'legal owner' yet will be deemed (i.e., treated) as owner of the property:
 - (a) A person who has transferred property to Spouse or Minor Child without adequate consideration.
 - (b) Holder of an Impartible Estate.
 - (c) Property held by a Member of Co-operative Society or company or Association of Persons, who has been allotted with the property under any Housing Scheme of the Society or Company or AOP.
 - (d) A person who has acquired property under a Power of Attorney Transaction.
 - (e) A person who has acquired a property on lease for a term of 12 years or more.

[A detailed discussion of ‘deemed ownership’ is made under the head “Income from House Property].

8. When a tenant of a property sub-lets the property and earns rental income, it is not ‘income from house property’ since the tenant is not the ‘owner of the property’.
9. The house property owned by the assessee must not be used by the assessee for any business or profession carried on by him as a proprietor, or by a firm in which he is a partner.
10. Where a house property owned by the assessee is let out by him to the employees of the business carried on by him, the income from such property is ‘Income from House Property’ when such letting out is **not** subservient and incidental to the business of the assessee. However, where such letting out is subservient and incidental to the business of the assessee, income from letting out property to employees is charged under the head ‘income from business or profession’.

CHARGEABILITY UNDER THE HEAD “INCOME FROM BUSINESS OR PROFESSION”

8.4

An income is chargeable under the head “Business or Profession” when it is specified or when it fulfills the conditions given, under section 28 of the Income Tax Act, 1961.

The following are the incomes included under section 28, by the Act:

Sl. No.	Section	Income specifically chargeable under this head
1.	28(i)	Profits and gains of any business/profession carried on by assessee, <i>at any time during the previous year</i>
2.	28(ii)	Compensation received on termination of or modification in terms / conditions of management/office/agency or on compulsory acquisition
3.	28(iii)	Income of trade, professional or similar association from specific service, performed for its members
4.	28(iiiia)	Profits on sale of licence granted under the Imports (Control) Order, 1955. Or profit on transfer of Duty Entitled Pass Book and Duty Free Replenishment Certificate
5.	28(iiib)	Cash assistance against export
6.	28(iiic)	Customs or excise duty drawback
7.	28(iiid)	Profit on transfer of the Duty Entitlement Pass Book Scheme, being the Duty Remission Scheme under the export and import policy formulated and announced under section 5 of the Foreign Trade (Development and Regulation) Act, 1992
8.	28(iiie)	Profit on the transfer of the Duty Free Replenishment Certificate, being the Duty Remission Scheme under the export and import policy formulated and announced under section 5 of the Foreign Trade (Development and Regulation) Act, 1992

Sl. No.	Section	Income specifically chargeable under this head
9.	28(iv)	Value of any benefit/perquisite arising from business or exercise of profession
10.	28(v)	Interest, salary, etc., to a partner of a firm to the extent allowed u/s 40(b) to the firm
11.	28(va)	Any sum received or receivable, in cash or kind, under an agreement (a) for not carrying out any activity in relation to any business or profession or (b) for not sharing any know-how, patent, copyright, trade mark, lince, franchise or any other business or commercial right of similar nature or information or technique likely to assist in the manufacture or processing of goods or provision for services.
12.	28(vi)	Sum received under Keyman insurance policy including bonus.
13.	28(vii)	Any sum, whether received or receivable, in cash or kind, on account of any capital asset (other than land or goodwill or financial instrument) being demolished, destroyed, discarded or transferred, if the whole of the expenditure on such capital asset has been allowed as a deduction under section 35AD.
14.	28(Expl. 2)	Income from speculative transactions.

Notes:

- Section 28(i) sets out the conditions to be fulfilled for charging an income under the head 'business and profession'. According to this clause, an income can be charged under the head "business and profession" when—
 - The income is a 'profit or a gain' (i.e., excess of income over expenditure);
 - Such profit or a gain is from 'business or profession' (not from sale of assets etc.);
 'Business' refers to a **continuous activity** of buying and selling or making and selling of goods, irrespective of the scale of operations. For tax purposes, 'business' includes trade and commerce.
 'Profession' refers to an activity carried out based on qualification or inherent skills. For tax purposes, 'profession' includes 'vocation'.
 - Such 'business or profession' must be carried on by the assessee;
 - It must be carried on by the assessee at any time during the previous year. That is, the business or profession need not be carried on by the assessee for the entire previous year. However, there are certain exceptions wherein, even though the business or profession is not carried on by the assessee during the previous year, the income can be charged under this head, when the other conditions are fulfilled. A detailed discussion of such exceptions is made in the chapter 'Income from Business or Profession'.
- Section 28(i), as explained above, is considered as 'narrow' chargeability. The other incomes given under section 28 are explained under the head 'Income from Business or Profession'.

CHARGEABILITY UNDER THE HEAD “CAPITAL GAINS”

8.5

An income is chargeable under the head “Capital Gains” when the income is a ‘gain’ on ‘transfer’ of ‘capital asset’.

For understanding the chargeability under this head, it is essential to understand the meaning of the terms ‘capital asset’ and ‘transfer’.

8.5.1 Capital Asset

According to Section 2 (14), Capital asset means property of any kind, whether fixed or circulating, movable or immovable, tangible or intangible. Besides, it includes the following:

- (a) Any rights in or in relation to an Indian company, including rights of management or control or any other rights whatsoever;
- (b) property of any kind held by the assessee, whether or not in connection with business or profession;
- (c) any securities held by a Foreign Institutional Investor which has invested in such securities in accordance with the regulations made under the Securities and Exchange Board of India Act, 1992 but does not include—
 1. Stock in trade (other than securities referred to above), or raw material or consumable stores held for the purpose of business.
 2. Personal movable effects other than jewelry, archeological collection, drawings, paintings, sculptures or work of Art.
 3. Agricultural land in a rural area in India (as given below).
 4. Specified Gold Bonds.
 5. Special Bearer Bonds of 1991.
 6. Gold Deposit Bonds issued under Gold Deposit Scheme, 1999 and **Gold Deposit Certificates issued under Gold Monetisation Scheme, 2015.**

Notes:

1. Securities

As per section 2(h) of Securities Contracts (Regulation) Act, 1956, unless the context otherwise requires, “securities” include—

- (a) shares, scripts, stocks, bonds, debentures, debenture stock or other marketable securities of a like nature in or of any incorporated company or other body corporate;
- (b) derivative;
- (c) units or any other instrument issued by any collective investment scheme to the investors in such schemes;
- (d) security receipt as defined in clause (zg) of the Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002;
- (e) units or any other such instrument issued to the investors under any mutual fund scheme;

- (f) any certificate or instrument (by whatever name called), issued to an investor by any issuer being a special purpose distinct entity which possesses any debt or receivable, including mortgage debt, assigned to such entity, and acknowledging beneficial interest of such investor in such debt or receivable, including mortgage debt, as the case may be;
 - (g) Government securities;
 - (h) such other instruments as may be declared by the Central Government to be securities; and
 - (i) rights or interest in securities.
2. Any property of the assessee, for whatever purpose it is used, other than the six exceptions given above, is a 'capital asset'.
 3. Profit on transfer of 'stock-in-trade, etc' is income from business.
 4. Jewellery, archeological collection, drawings, paintings, sculpture or work of art are capital assets.
 5. Agricultural Land in rural area

It means:

- (a) if situated in any area which is comprised within the jurisdiction of a municipality (whether known as a municipality, municipal corporation, notified area committee, town committee or by any other name) and its population should be less than 10,000; or
- (b) if situated outside the limits of municipality etc., at a distance, measured aially:
 - (i) being more than two kilometers, from the local limits of any municipality or cantonment board referred to in item (a) and which has a population of more than 10,000 but not exceeding 1,00,000, or
 - (ii) being more than six kilometers, from the local limits of any municipality or cantonment board referred to in item (a) and which has a population of more than 1,00,000 but not exceeding 10,00,000, or
 - (iii) being more than eight kilometers, from the local limits of any municipality or cantonment board referred to in item (a) and which has a population of more than 10,00,000.

The expression 'population' means population according to the last preceding census of which the relevant figures have been published before the first day of the previous year.

8.5.2 Transfer

According to Section 2(47), **Transfer** includes—

- (a) Sale, exchange or relinquishment of the asset, or
- (b) Extinguishment of any rights therein, or
- (c) Compulsory acquisition thereof under any law, or
- (d) Conversion of capital asset into stock-in-trade, or

8.10 • Income Tax - I

- (e) Redemption of zero coupon bond, or
- (f) Any transaction involving the possession of any immovable property in part performance of a contract, or
- (g) Any transaction which has the effect of transferring or enabling the enjoyment of any immovable property,
- (h) Disposing of or parting with an asset or any interest therein or creating any interest in any asset in any manner whatsoever.

According to Section 47, the following transactions are **not regarded as transfer**:

1. Distribution of asset in kind by a company to its shareholders at the time of liquidation.
2. Distribution of capital asset on total or partial partition of Hindu Undivided Family.
3. Transfer of capital asset under a gift or will or an irrevocable trust.
4. Transfer of a capital asset by a company to its 100 per cent subsidiary company.
5. Transfer of a capital asset by a 100 per cent subsidiary company to its holding company.
6. Transfer of capital assets in a scheme of amalgamation.
7. Transfer of shares in Indian company held by a foreign company to another foreign company under a scheme of amalgamation of the two foreign companies.
8. Transfer of capital assets in a scheme of amalgamation of a banking company with a banking institution.
9. Transfer in a demerger of a capital asset by the demerged company to resulting company.
10. Transfer of shares held in an Indian company by a demerged foreign company to the resulting foreign company.
11. Transfer of shares of a foreign company, deriving its value substantially from the shares in an Indian company, in a scheme of amalgamation or demerger, where the amalgamating/demerged and amalgamated/resulting companies are foreign companies.
12. Any transfer in a business reorganization, of a capital asset by the predecessor co-operative bank to the successor co-operative bank.
13. Any transfer by a shareholder, in a business reorganization, of a capital asset being a share or shares held by him in the predecessor co-operative bank if the transfer is made in consideration of the allotment to him of any share or shares in the successor co-operative bank.
14. Transfer or issue of shares by the resulting company, in a scheme of demerger, to the shareholders of the demerged company.
15. Allotment of shares in amalgamated company in lieu of shares held in amalgamating company.
16. Transfer of capital asset (being Foreign Currency Convertible Bonds or GDR) by a non-resident to another non-resident.

17. Transfer of a capital asset (being a Government Security carrying periodic payment of interest) made outside India through an intermediary dealing in settlement of securities by a non-resident to another non-resident.
18. Redemption of Sovereign Gold Bond issued by RBI under the Sovereign Gold Bond Scheme, 2015, by an Individual.
19. Transfer of agricultural land in India before March 1, 1970.
20. Transfer of a capital asset (being work of art, manuscript, painting etc) to Government/ University/national museum etc.
21. Transfer by way of conversion of bonds or debentures into shares.
22. Transfer by way of conversion of bonds [referred to in section 115AC(1)(a)] into shares or debentures of any company.
23. Transfer by way of exchange of a capital asset being membership of a recognized stock exchange for shares of a company.
24. Transfer of land by a sick industrial company which is managed by its workers' co-operative.
25. Transfer of a capital asset by a firm to a company in case of conversion of firm into a company.
26. Transfer of a capital asset, being a membership right held by a member of a recognized stock exchange in India.
27. Transfer of capital asset or intangible asset by a Private Limited Company or a non-listed company to Limited Liability Partnership shall not be regarded as a transfer.
28. Transfer of a capital asset to a company in case of conversion of proprietary concern into a company.
29. Transfer involving in a scheme of lending of securities.
30. Transfer of a capital asset in a transaction of reverse mortgage made under a scheme notified by the Government.
31. Transfer of a capital asset (being share of a special purpose vehicle) to a business trust in exchange of units allotted by that trust to the transferor.
32. Any transfer by a unit-holder of a capital asset, being a unit or units, held by him in the consolidating plan of a mutual fund scheme, made in consideration of the allotment to him of a capital asset, being a unit or units, in the consolidated plan of that scheme of the mutual fund.

So, under the head 'capital gains' the process for identifying chargeability is—

1. Ascertain whether the transaction carried out by the assessee is 'transfer' (That is, whether the transaction carried out by the assessee is within the meaning of Section 2(47) and outside the purview of Section 47).
2. If yes, ascertain whether the transfer is of a 'Capital Asset' (That is, an asset as defined under Section 2(14), and is not an asset under the exceptions).

3. If yes, the outcome of the transaction is 'capital gain' and hence, must be charged under the head "Capital Gains".

8.6 CHARGEABILITY UNDER THE HEAD "INCOME FROM OTHER SOURCES"

An income is chargeable under this head when the following conditions are fulfilled:

- There is an "income".
- The income should **not** be exempt from tax under Sections 10 to 13A.
- The income is **not** chargeable under other heads of income.

In short, an income is taxable under this head when it is not an exempted income, and not chargeable under any other earlier heads of income. On account of this, this head is also called "**Income from Residuary Sources**".

Illustration 1 Problem on ascertaining the head of income under which a taxable income must be charged

State the head of income under which the following incomes must be charged to tax:

Sl. No.	Income
1.	Salary income as an employee at WIPRO Ltd.
2.	Free Accommodation provided by employer
3.	X is Director (Marketing) of ABC Ltd. He gets ₹1,00,000 during previous year 2017-18 for attending Board Meetings.
4.	Y is an Independent Director of ABC Ltd. He gets ₹2,00,000 during previous year 2017-18 for attending Board Meetings.
5.	Dr. Nagaraju is a Professor in the Management Department of Bangalore University. He is invited by Mangalore University for evaluation work and paid ₹25,000 as the remuneration.
6.	Salary received by a partner from his partnership firm.
7.	Salary received by Members of Parliament and Members of Legislative Assembly.
8.	Pension received after retirement from services.
9.	Pension received from Pension Fund Scheme of Life Insurance Corporation of India.
10.	Balu is appointed by VITTAM Recording Company for writing lyrics, singing songs and marketing cassettes, for which he is paid a monthly remuneration of ₹5,00,000.
11.	Sonu is approached by Producers for singing songs for their forthcoming movie in a regional language. He is paid a remuneration of ₹50,000 per song.
12.	Rental income from letting out residential property.
13.	Rental income from letting out commercial complex.
14.	Rental income of a dealer in Properties.
15.	Rental income received by Sheela, tenant of a two-storied property in Bangalore, from sub-letting ground floor.

Sl. No.	Income
16.	Rental income of Ramesh from letting out vacant site in J P Nagar for conducting functions and rituals by the residents of the lay-out.
17.	Profits from the business of dealing in Stationery.
18.	Profits from renting 'generators'.
19.	Mr. Balaji, running a photocopy business, has let-out his photo-copy machine to Z for 3 months, since he is travelling and not able to run his business during that period.
20.	Suresh is employed by MC GRAW HILL PUBLICATIONS to write books. 5% of sales revenue from the books is given as his remuneration by the Publisher.
21.	Raj writes 'Income Tax' books for MC GRAW HILL PUBLICATIONS. 10% of sales revenue from the books is given by the Publisher to Raj as his remuneration.
22.	Interest on Debentures.
23.	Interest on Debentures received by a dealer in Securities.
24.	Winnings from Lottery.
25.	Winnings from unsold and unclaimed Lottery by a Lottery agent.
26.	Interest on Bank Deposits.
27.	Compensation received by Michael for cancellation of his KFC Franchise by the Company.
28.	Compensation received for compulsory acquisition of land belonging to the assessee.
29.	Interest received on enhanced compensation for compulsory acquisition of assessee's asset.
30.	Cash Gifts received by the assessee.

Solution:**Statement showing Classification of Income under Various Heads**

Sl. No.	Income	Head of Income
1.	Salary income as an employee at WIPRO Ltd.	Income from Salary
2.	Free Accommodation provided by employer	Income from Salary
3.	X is Director (Marketing) of ABC Ltd. He gets ₹1,00,000 during previous year 2017-18 for attending Board Meetings.	Income from Salary (since X is an employee of the Company)
4.	Y is an Independent Director of ABC Ltd. He gets ₹2,00,000 during previous year 2017-18 for attending Board Meetings.	Income from Other Sources (since Y is not an employee of the Company)
5.	Dr. Nagaraju is a Professor in the Management Department of Bangalore University. He is invited by Mangalore University for evaluation work and paid ₹25,000 as the remuneration.	Income from Other Sources (since the remuneration is 'based on employment', but payment is not by employer)

8.14 • Income Tax - I

Sl. No.	Income	Head of Income
6.	Salary received by a partner from his partnership firm	Income from Business (since the Partner is both 'employer' and 'employee'. Further, Section 28(iv) specifies such income as 'Income from Business')
7.	Salary received by Members of Parliament and Members of Legislative Assembly	Income from Other Sources (since they are not employees, but members)
8.	Pension received after retirement from services	Income from Salaries
9.	Pension received from Pension Fund Scheme of Life Insurance Corporation of India	Income from Other Sources
10.	Balu is appointed by VITTAM Recording Company for writing lyrics, singing songs and marketing cassettes, for which he is paid a monthly remuneration of ₹5,00,000	Income from Salaries
11.	Sonu is approached by producers for singing songs for their forthcoming movie in a regional language. He is paid a remuneration of ₹50,000 per song	Income from Profession (if revenue from the activity of 'Singing' forms substantial part of his revenues) Or Income from Other Sources (if 'Singing' is not the main activity carried on by him)
12.	Rental income from letting out residential property	Income from House Property
13.	Rental income from letting out commercial complex	Income from House Property
14.	Rental income of a dealer in properties	Income from House Property (the fact that the assessee is a dealer in properties is irrelevant, if all the conditions under the head 'Income from House Property' is fulfilled)
15.	Rental income received by Sheela, tenant of a two-storied property in Bangalore, from sub-letting of ground floor	Income from Other Sources (since Sheela is not the owner of the property)
16.	Rental income of Ramesh from letting out vacant site in J P Nagar for conducting functions and rituals by the residents of the lay-out	Income from Other Sources (since the property let-out is not a house property)
17.	Profits from the business of dealing in Stationery	Income from Business

Sl. No.	Income	Head of Income
18.	Profits from renting 'generators'	Income from Business
19.	Mr. Balaji, running a photocopy business, has let-out his photo-copy machine to Z for 3 months, since he is travelling and not able to run his business during that period.	Income from Other Sources (since assessee is not engaged in the 'business' of letting out photo-copy machines)
20.	Suresh is employed by MC GRAW HILL PUBLICATIONS to write books. 5% of sales revenue from the books is given as his remuneration by the publisher.	Income from Salaries (since Suresh is employed by the Company, the remuneration is received by him is "Income from Salaries")
21.	Raj writes 'Income Tax' books for MC GRAW HILL PUBLICATIONS. 10% of sales revenue from the books is given by the Publisher to Raj as his remuneration	Income from Other Sources (Royalty Income)
22.	Interest on Debentures	Income from Other Sources
23.	Interest on Debentures received by a dealer in Securities	Income from Other Sources (the fact that assessee is a dealer in Securities is irrelevant – interest income must be considered under the head "Income from Other Sources")
24.	Winnings from Lottery	Income from Other Sources (Casual Income)
25.	Winnings from unsold and unclaimed Lottery by a Lottery agent	Income from Business (in accordance with the decision in the case ' Director of State Lotteries Vs. CIT ')
26.	Interest on Bank Deposits	Income from Other Sources
27.	Compensation received by Michael for cancellation of his KFC Franchise by the Company	Income from Business [According to Section 28(ii)]
28.	Compensation received for compulsory acquisition of land belonging to the assessee	Capital Gains [According to Section 2(47)]
29.	Interest received on enhanced compensation for compulsory acquisition of assessee's asset	Income from Other Sources
30.	Cash Gifts received by the assessee	Income from Other Sources

Note: Gifts (i.e., receipts without consideration) is an income according to Income Tax Act. A detailed discussion of the same is made under the head "Income from Other Sources".

SUMMARY

- Once the taxable incomes are identified, the next step in making assessment is – classifying taxable incomes under appropriate head of income.
- Under Income Tax Act, 1961 – taxable incomes must be classified under five different heads viz., Income from Salaries, Income from House Property, Income from Business or Profession, Capital Gains and Income from Other Sources.
- An income is chargeable under a particular head of income on fulfillment of certain conditions under that head. This is called chargeability.
- An income is chargeable under the head “Income from Salaries” when the assessee gets the income from his “employer” and such payment is made by employer to employee “out of employment”.
- An income is chargeable under the head “Income from House Property” when the income is from a property (consisting of buildings and land appurtenant thereto) which is owned by the assessee, and not used by him for his business or profession.
- An income is chargeable under the head “Business or Profession” when the income is a ‘profit or a gain’ from a ‘business or profession’ carried on by the assessee during the previous year, or when the income is specified under section 28.
- An income is chargeable as “Capital Gain” when the income is a “Gain” on “Transfer” of “Capital Asset”.
- An income which does not fulfill the conditions under the first four heads of income, must be considered under the head “Income from Other Sources”.

THEORY QUESTIONS

Section A Type Questions

1. List the heads of Income as classified under the Income Tax Act, 1961.
2. State the conditions for considering an income under the head “Salaries”.
3. When is an income chargeable under the head “Income from House Property”?
4. What is the meaning of ‘House Property’?
5. Explain the terms ‘Business’ and ‘Profession’.
6. State the general conditions prescribed under section 28(i) for charging an income under the head “Business and Profession”.
7. List any six incomes under section 28.
8. When is an income chargeable as ‘Capital Gains’?
9. What is a ‘capital asset’? List the exceptions for ‘capital asset’.
10. List any four transactions regarded as ‘transfer’.
11. List any six transactions not regarded as ‘transfer’.
12. State the conditions for charging an income under the head “Other Sources”.

Section B Type Questions

1. Explain the chargeability under the heads – Salaries, House Property and Other Sources.
2. List the incomes covered under section 28 of the Income Tax Act, 1961.
3. Explain the term 'Capital Asset', along with its exceptions.
4. What is 'Transfer' under section 2(47)?
5. List any ten transactions not regarded as 'transfer'.

Section C Type Questions

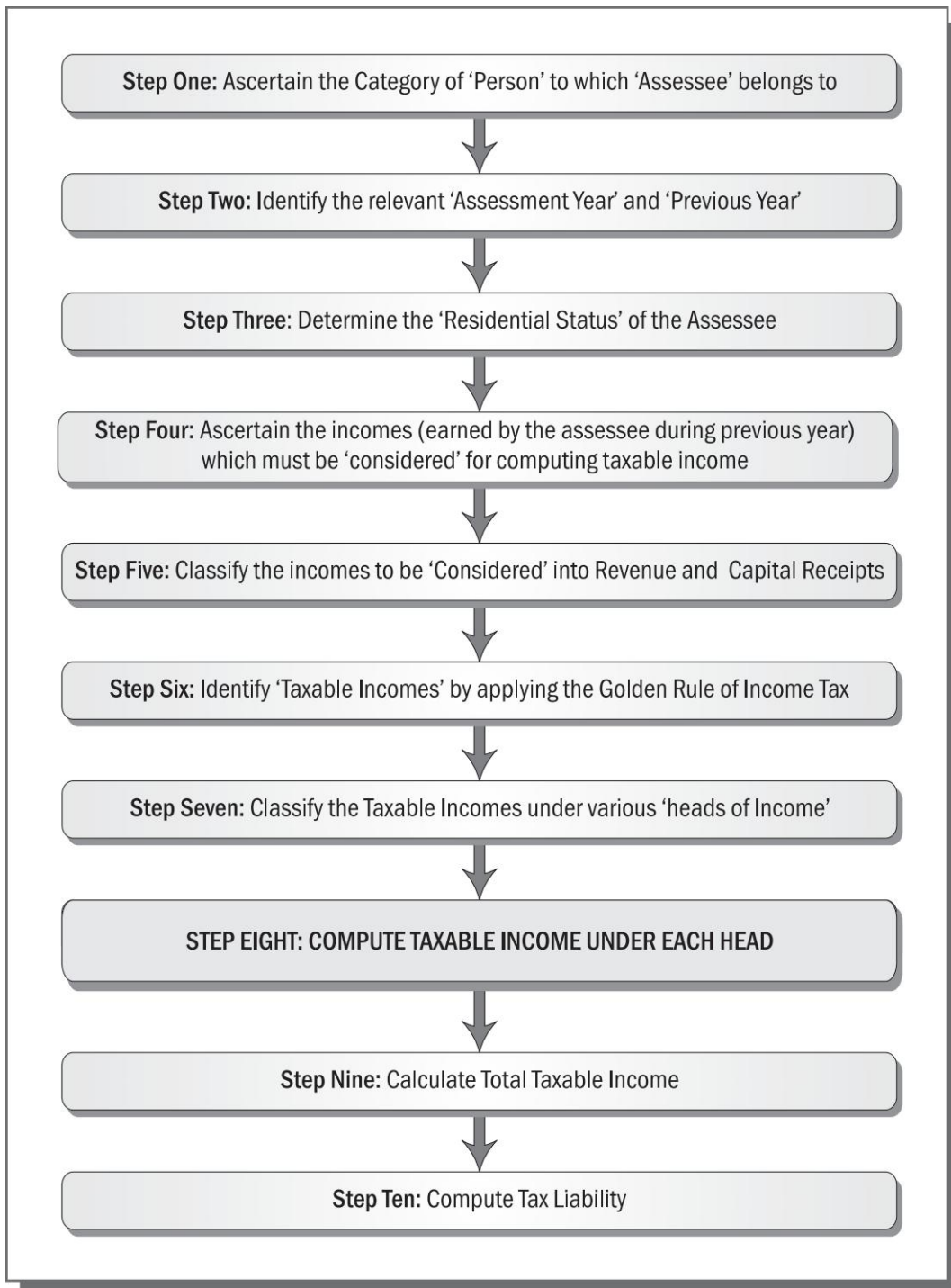
1. Explain the 'chargeability' of income under various heads of income, according to the Income Tax Act, 1961.

EXERCISES

Identify the head of income under which the following incomes are chargeable:

1. Free transport facility provided by employer.
2. Rent charged by X for sub-letting a portion of his rented house.
3. Profit on sale of watches.
4. Compensation received for cancellation of contract by a customer.
5. Compensation received for compulsory acquisition of assessee's site.
6. Interest on Fixed Deposit in a Bank.
7. Interest on Debentures.
8. Dividends from Foreign Companies.

(Ans: (1) *Income from Salaries*, (2) *Income from Other Sources*, (3) *Business and Profession*,
(4) *Business and Profession*, (5) *Capital Gains*, (6) *Income from Other Sources*,
(7) *Income from Other Sources*, and (8) *Income from Other Sources*)



9

Computation of Taxable Income Under Each Head

CHAPTER OVERVIEW

- 9.1 Introduction
- 9.2 Income from Salaries – Chargeability
- 9.3 Income from Salaries – Basis of Charge
- 9.4 Format for Computing Taxable Salary
- 9.5 Provisions
- 9.6 Forms of Salary
- 9.7 Allowances
- 9.8 Deductions under Section 16.
- 9.9 Provident Fund
- 9.10 Perquisites
- 9.11 Profits in Lieu of Salary

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- In the process of making assessment, the next step is to compute taxable income under each 'head of income'. This chapter explains computation of taxable income under the first head – "Income from Salaries".

INTRODUCTION

9.1

Computation of taxable income under each head involves three aspects, viz.,

1. When?
2. How?
3. How Much?

The 'When?' aspect is about the '**Chargeability**' of income under the head. This aspect explains the conditions to be fulfilled for charging an income under the head. (This has been explained in Chapter Number Eight. However, additional information and detailed explanation is provided under each respective head).

The 'How?' aspect is about the '**Basis of Charge**' of the income under each head. This aspect explains the criterion based on which the chargeability of income is decided. The 'How?' aspect is most crucial in computing taxable income under each head. The 'Basis of Charge' explained under each head, ensures uniformity in tax treatment.

The 'How Much?' aspect is about the '**Formats and Provisions**' for computing the taxable income under each head.

Under each head of income, the discussion is shown in the following order:

1. Chargeability.
2. Basis of Charge.
3. Formats and Provisions.

INCOME FROM SALARIES

CHARGEABILITY

9.2

According to section 15 of the Income Tax Act, an income is chargeable under the head “Salaries” when—

- (a) The relationship between ‘payer’ and ‘assessee’ is in the nature of ‘employer-employee’; and
- (b) The payment made by ‘employer’ to assessee is ‘out of employment’.

Notes:

1. An ‘employer-employee’ relationship is bound by ‘service agreement’.
2. A contractual relationship is not ‘employer-employee’ relationship. For example, relationship between a Chartered Accountant and Client, Doctor and Patient, Lawyer and Client, etc., is governed by ‘contract’ (whether expressed or implied), and not by ‘service agreement’.
3. Once governed by ‘service agreement’, ‘employer-employee’ relationship comes into existence, irrespective of the qualification and other traits of the employee. A person may be a Medical Practitioner (Doctor) by qualification. However, once he is employed in a Medical Institution (Hospital etc.), he becomes an ‘employee’ and the payment by the hospital to him for services rendered must be considered as ‘income from salary’ and not as ‘income from profession’.
4. Only payments made by ‘employer’ to ‘employee’ based on ‘employment’ can be considered as ‘income from salary’. For example, suppose an employee of Reliance Industries Ltd., has invested in Debentures of the Company. The interest on debentures paid by the company each year is not ‘income from salary’ to the assessee, although he is employee of the company, since the payment is not ‘out of employment’ (i.e., it is not based on his employment in the company). The same is the treatment even when the debentures are allotted by the Company.
5. Any income arising ‘out of employment’, but not from ‘employer’ is not ‘income from salary’. For example, suppose a Professor of Commerce has been chosen by Bangalore University for setting question paper, and the selection is based on long service rendered in his college, which is affiliated to the said University. The remuneration for setting paper

is not 'income from salary' though it is 'out of employment' (i.e., based on his employment) since the payment of remuneration is not by his 'employer'.

6. Unless both the conditions specified under section 15 are fulfilled, an income cannot be charged under the head "Salaries".

BASIS OF CHARGE

9.3

Under this head, the income is chargeable on '**accrual**' basis or '**receipt**' basis, whichever happens earlier.

Notes:

1. Salary is said to 'accrue' when an employee has rendered his services to the employer for a specified period. For example, In India, salary accrues when employee has rendered service for a given month.
2. Salary is liable for tax, once it accrues to the employee, irrespective of whether it is received or not.
3. Suppose, an employee has rendered service for the entire previous year 2017-18, but has not received any payment from employer due to financial constraints of the employer. Since, employee has rendered service, salary has 'accrued' to him and hence taxable, even though it has not been received.
4. Where salary is received by the employee before its accrual, then it is taxable on 'receipt' basis.
5. Suppose, during March 2018 the same employee in the above example, receives salary of April and May, in advance. Then, salary is said to be received, without accruing. The same will be taxable for the previous year 2017-18 (i.e., Assessment Year 2018-19).
6. In the above example, the employee will be chargeable for 14 months' salary during previous year 2017-18, of which, 12 months' salary is on 'accrual' basis and 2 months' salary on 'receipt' basis.
7. Where an employee **voluntary forgoes** his salary to his employer, he is still liable for tax, since salary has accrued to him. His forgoing of salary merely becomes an application of his income.
8. However, where an employee **surrenders his salary to the Government**, despite being accrued to the employee, the salary income is not taxable.

FORMAT FOR COMPUTING TAXABLE SALARY

9.4

Computation of Taxable Salary

Assessee: (Name of the Employee) Assessment Year: 2018-19
 Status: (Residential Status) Previous Year: 2017-18
 Category: (Government/Semi-Government/Non-Government)

	₹
Forms of Salary	XXX
Allowances and Provident Fund	XXX
Perquisites	XXX
Profits in Lieu of Salary	XXX
Gross Salary	XXX
Deductions U/s 16:	
(ii) Entertainment Allowance XXX	
(iii) Employment Tax XXX	
-----	XXX
Taxable Salary	XXX

Notes:

- The tax-treatment for 'salary incomes' received by an employee depends upon the category of his employment – i.e., whether he is a government employee or a semi-government employee or a non-government employee. Hence, it must be ascertained before commencement of computation of taxable income.
- An employee is a 'Government Employee' when he is working in an organisation which is owned, controlled and managed by the Government or Government Authority. Example of Government Organisations – P & T Department, Indian Railways, Government Colleges, Secretariat, RBI, etc.
 An employee is a 'Semi-Government Employee' when he is working in an organisation which is not owned by the Government, but controlled by the Government and managed by the body/persons appointed by the Government. Example of Semi-Government Organisations – Statutory Corporations like LIC, GIC, HAL, BEL etc., Nationalised Banks, Aided Colleges, Local Authority, etc,
 An employee is a 'Non-Government Employee' or a 'Private Employee' when he is working in an organisation which is neither owned nor managed by the Government. Examples of Non-Government Organisations – Companies like Ranbaxy, Wipro, etc., Proprietary concerns, Partnership Firms, Societies, Trusts, etc. (Note – Private Colleges are managed by Trusts, and hence are non-government organisations).
- In any later discussion in this chapter, the term 'Other than Government Employees' includes both 'semi-government employees' and 'non-government employees'.

4. The format above lists out only the major heads under the head “Salaries”. Various items under each head, their meaning and tax treatment have been explained in detail, in the following pages.
5. The numbers mentioned under section 16 are not serial numbers, but clause numbers under which the respective deductions are covered. Currently, deduction under clause number (ii) and (iii) only are available. Deduction under section 16(i) has been removed.
6. Where an employee has rendered services to more than one employer during the previous year (at the same time or separately), the same format has to be repeated up to ‘Gross Salary’.

PROVISIONS

9.5

The tax provisions for incomes under this head are grouped under the following heads:

- A. Forms of Salary
- B. Allowances
- C. Deductions under section 16
- D. Provident Fund
- E. Perquisites
- F. Profits in Lieu of or in Addition to Salary

Each of the above has been discussed in detail in this chapter.

FORMS OF SALARY

9.6

‘Forms of Salary’ refers to the various forms of remuneration or compensation paid by employer to employee for the services rendered by employee – payable either during service period or at the time of retirement or after retirement.

The following is the broad list of incomes under this head:

1. Basic Salary
2. Advance Salary
3. Dearness Pay
4. Bonus
5. Commission
6. Fees
7. Interim relief
8. Gratuity
9. Leave salary
10. Pension

The meaning and tax-treatment of each of the above items has been given as follows:

9.6.1 Basic Salary

It refers to the basic remuneration the employee is entitled to, for the services rendered by him to his employer organisation. This form of salary forms the basis for calculating many other benefits to the employee and hence, it is called 'Basic' Salary.

'Basic Salary' includes only the basic salary of *relevant previous year* and it is **completely taxable**.

The amount of basic salary may be given as a fixed amount per month or per annum; or given as a pay-scale. When given as a *pay-scale*, the 'basic salary' for the relevant previous year must be ascertained. The following illustration explains the calculation of basic salary, when a pay-scale is given.

Illustration 1 Problem on Calculation of Basic Salary

Mr. Dayanand joined the services of 'Sevabharathi' on 01.11.2010, in the pay scale of ₹8,000 – 275 – 9,100 – 550 – 10,750 – 825 – 13,225 per month. Calculate his basic salary for the previous years 2016-17 and 2017-18, if the salary falls due on:

- last date of each month; and
- first of the following month, but received on fifth.

Solution:

The pay-scale given is– ₹8000 – 275 – 9100 – 550 – 10750 – 825 – 13225 per month.

It is read as follows:

During the first year of service, the monthly salary of Dayanand is ₹8000 per month.

For the second year of service, the monthly salary will be ₹8,275 per month.

Similarly, ₹8,550 per month for the third year, ₹8,825 per month for the fourth year, ₹9,100 per month for the fifth year, will be the basic salary.

Once the basic salary is ₹9,100 per month, the next increment will not be ₹275, but ₹550 per month. Hence, for the sixth year of service, the basic salary will be ₹9,650; and so on.

The same is presented in the below table up to the relevant previous year–

Period	Basic Salary per month (₹)
From November 2010 to October 2011	8,000
From November 2011 to October 2012	8,275
From November 2012 to October 2013	8,550
From November 2013 to October 2014	8,825
From November 2014 to October 2015	9,100
From November 2015 to October 2016	9,650
From November 2016 to October 2017	10,200
From November 2017 to October 2018	10,750

Notes:

- The calculation of 'basic salary' must be considered from the calendar month of joining the service, and not the date of joining the service. Irrespective of the date on which employee joins service, the salary for the calendar month of joining the service will be same.
- Where Dayanand had joined service on 21st November 2010, he will be paid 10 days' salary @ ₹8000 per month for that month.

Calculation of Basic Salary under situation (a):

'Salary falling due on the last date of each month' means salary for each month accrues in the month of rendering service. That is, for the month of April 2017 – salary accrues in April 2017, and so on.

Salary being taxable on accrual basis, the salary that accrues during the relevant previous year must be considered. Since, salary for each month accrues in the same month of service, basic salary will be 'salary of April to March'.

For previous year 2016-17, the basic salary is ₹9,650 per month from April 2016 to October 2016 and ₹10,200 per month from November 2016 to March 2017. So, the basic salary is–

$$[₹9,650 \times 7] + [₹10,200 \times 5] = ₹1,18,550.$$

For previous year 2017-18, the basic salary is ₹10,200 per month from April 2017 to October 2017 and ₹10,750 per month from November 2017 to March 2018. So, the basic salary is–

$$[₹10,200 \times 7] + [₹10,750 \times 5] = ₹1,25,150.$$

Calculation of Basic Salary under situation (b):

'Salary falling due on the first of the following month' means salary for each month of service accrues in the following month. That is, Salary for January 2018, accrues in February 2018 and so on. The date of the following month on which the salary accrues and the date on which the salary is received, are irrelevant.

In the month of April of any year, the salary that accrues is that of the month of March; similarly, in the month of May of any year, the salary that accrues is that of the month of April. The salary for the month of January accrues in the month of February, that for February in the month of March and the salary for the month of March, accrues in the month of April of the next financial year.

Salary being taxable on accrual basis, the salary that accrues during the relevant previous year must be considered. During any previous year of April to March, the salary that accrues is of the preceding month – i.e., March to February. Hence, under this situation, the salary from the month of March to the following February must be considered.

For previous year 2016-17, the basic salary is ₹9,650 per month from March 2016 to October 2016 and ₹10,200 per month from November 2016 to February 2017. So, the basic salary is:

$$[₹9,650 \times 8] + [₹10,200 \times 4] = ₹1,18,000.$$

For previous year 2017-18, the basic salary is ₹10,200 per month from March 2017 to October 2017 and ₹10,750 per month from November 2017 to February 2018. So, the basic salary is:

$$[₹10,200 \times 8] + [₹10,750 \times 4] = ₹1,24,600.$$

9.6.2 Advance Salary

‘Advance Salary’ refers to the basic salary of the future period, received during the relevant previous year. It represents salary received before its accrual. Any advance salary received by assessee, during the relevant previous year, is **completely taxable**.

9.6.3 Dearness Pay

‘Dearness Pay’ is a part of basic salary, paid in a different nomenclature. It is **completely taxable**.

9.6.4 Bonus

‘Bonus’ is an incentive given to the employee. It represents share of profits distributed to employee, by the employer. It is **completely taxable on receipt basis**. That is, the amount of bonus *received* by the employee during the relevant previous year is taxable, irrespective of the period to which the bonus belongs to.

9.6.5 Commission

‘Commission’ is another form of remuneration given to employee. It is also called variable pay. It may be a fixed amount or percentage of sales or profits or production etc. It is **completely taxable on receipt basis**. That is, the amount of commission *received* by the employee during the relevant previous year is taxable, irrespective of the period to which the commission belongs to.

9.6.6 Fees

‘Fees’ refers to any extra remuneration for additional services rendered by employee. For example, when the Managing Director of a company attends Board Meeting, he is paid ‘sitting fees’. This is remuneration for his additional duty of attending the meeting. It is **completely taxable**.

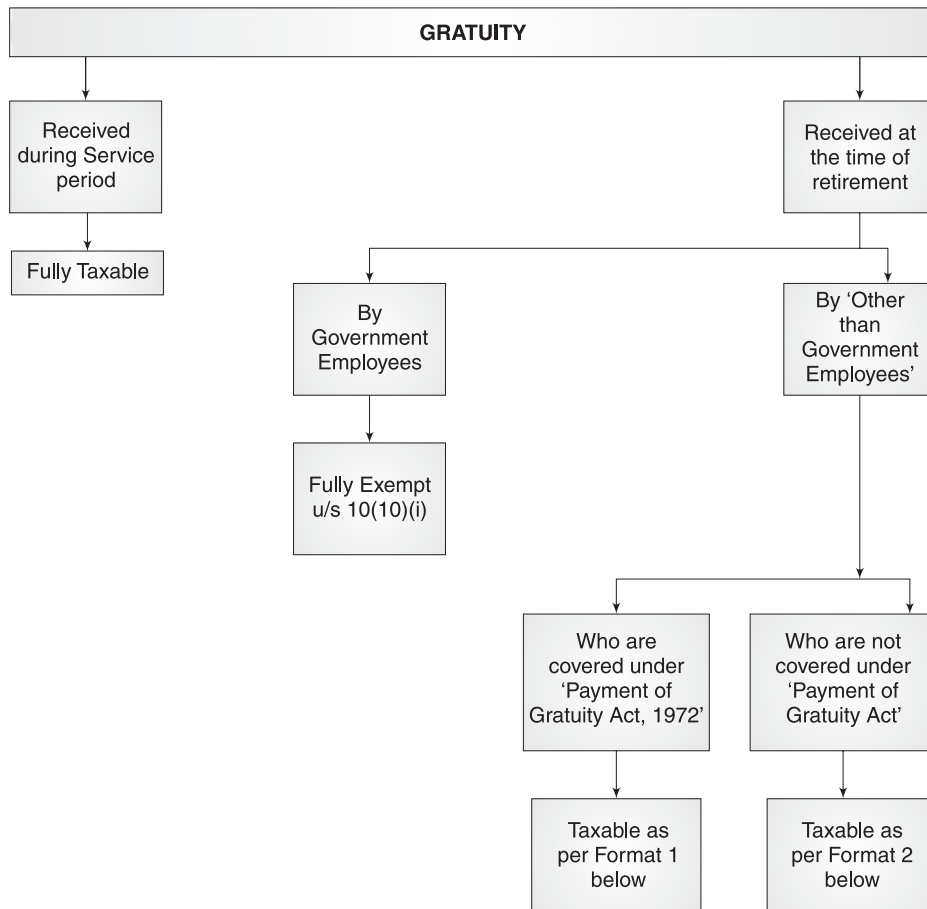
9.6.7 Interim Relief

‘Interim Relief’ has two meanings – ‘amount paid by employer to employee, for enabling employee to take pre-cautionary measures for protection from occupational hazards’; and ‘compensation for minor accident or injury to employee who continues to work despite the accident or injury’. Irrespective of its meaning, any interim relief received by employee is **completely taxable**.

9.6.8 Gratuity

‘Gratuity’ refers to payment made by employer to employee, for the meritorious service rendered by employee. It is paid to employee in gratitude for the services rendered by him to the employer organisation. It is usually paid at the time of retirement, although some organisations offer gratuity during service period of the employee.

The tax treatment for gratuity is summarised in the following chart:



Format One

This format for computing taxable gratuity is applicable to 'Other than Government Employees' who are **covered** under 'The Payment of Gratuity Act, 1972'.

The Payment of Gratuity Act, 1972 is applicable to the following–

- (a) Every factory, mine, oilfield, plantation, port and railway company;
- (b) Every shop or establishment within the meaning of any law for the time being in force in relation to shops and establishment in a State, in which ten or more persons are employed, or were employed, on any day of the preceding twelve months;
- (c) Such other establishments or class of establishments, in which ten or more employees are employed, or were employed, on any day of the preceding twelve months, as the Central Government may, by notification, specify in this behalf.

The format is as follows:

9.12 • Income Tax - I

	₹	₹
Actual Gratuity Received		XXX
Less: <i>Exempt under section 10(10)(ii), being least of the following:</i>		
(a) $15/26 \times \text{'Last drawn Salary'} \times \text{Number of years of service}$	XXX	
(b) Maximum Limit	10,00,000	
(c) Actual Gratuity Received	XXX	XXX
Taxable Gratuity		XXX

Notes:

- 15/26 in the above format represents half a month. Since, the maximum number of working days in a month is 26, it is represented so.
- Where the assessee is an employee of a seasonal establishment, 15/26 in the above format must be replaced by 7/26 – which represents quarter of a month.
- 'Last drawn salary' includes 'Basic Salary' and 'Dearness Allowance' for the last month of service of the employee. Basic Salary does not include overtime wages.
- Where the employee is remunerated on piece rate basis, 'last drawn salary' must be taken as 'average of basic salary and dearness allowance of the last 3 months of service'. (That is, total of basic salary and dearness allowance for last 3 months of service, divided by 3).
- The number of years of service must be **rounded off**. If the period of service is 6 months or less than 6 months, it must be ignored for this purpose. For example, suppose an employee had rendered 29 years and 8 months of service, the number of years of service for the above format purposes must be considered as 30 years. Where the actual service is for 29 years and 5 months, it must be considered as 29 years. In case the service rendered is for 29 years and 6 months, it must be considered as 29 years.
- The maximum exemption of ₹10,00,000 is for the life-time of the assessee and not for each time exemption is claimed. Where the assessee had earlier received any gratuity and such gratuity was exempt partly or fully, and when exemption is being calculated for gratuity received next time, the maximum exemption will be ₹10,00,000 as reduced by the amount of gratuity exempted earlier.
- The exemption in respect of gratuity would be available even if the gratuity is received by the widow, children or dependents of a deceased employee.

Format Two

This format for computing taxable gratuity is applicable to 'Other than Government Employees' who are **not covered** under 'The Payment of Gratuity Act, 1972'. The format is as follows:

	₹	₹
Actual Gratuity Received		XXX
Less: <i>Exempt under section 10(10)(iii), being least of the following:</i>		
(a) $1/2 \times \text{'Average Salary'} \times \text{Number of completed years of service}$	XXX	
(b) Maximum Limit	10,00,000	
(c) Actual Gratuity Received	XXX	XXX
Taxable Gratuity		XXX

Notes:

1. Only number of completed years of service must be considered. For example, where an employee, till his retirement, had rendered 23 years and 11 months of service, only 23 years must be considered.
2. The maximum exemption of ₹10,00,000 is for the life-time of the assessee and not for each time exemption is claimed. Where the assessee had earlier received any gratuity and such gratuity was exempt partly or fully, and when exemption is being calculated for gratuity received next time, the maximum exemption will be ₹10,00,000 as reduced by the amount of gratuity exempted earlier.
3. 'Average Salary' refers to **Total** of Basic Salary, Dearness Pay, Dearness Allowance (if it enters into retirement benefits) and Commission based on a fixed percentage of turnover achieved by employee for 10 months preceding the **month** of retirement of the employee, **divided by 10**.
4. Where an employee retires in the month of December 2017, February 2017 to November 2017 are the 10 months preceding the month of retirement. The date on which employee retired in December 2017, is irrelevant.
5. When Dearness Allowance is considered for computing contribution to retirement benefits like Provident Fund, it is said to be entering into retirement benefits. The arrangement regarding this will be given in service agreement. For example, when the service agreement states:
 - Contribution to Provident Fund is 10% of 'Basic Salary and DA' – then DA is said to be entering into retirement benefits;
 - Contribution to Provident Fund is 10% of 'Basic Salary' – then DA is not entering retirement benefits.
 - Contribution to Provident Fund is 10% of 'Basic Salary and 75% of DA' – then, 75% of DA is entering into retirement benefits.
6. Unless clearly stated or hinted, Dearness Allowance must be assumed as '**not entering into retirement benefits**'.
7. Considering Dearness Allowance for computing 'Average salary' only when it enters into retirement benefits is applicable only when the employee is **not covered** under 'The Payment of Gratuity Act'. In case of employees **covered** under 'The Payment of Gratuity Act', there is no condition to be fulfilled for considering Dearness Allowance in calculating 'last drawn salary'.
8. The exemption in respect of gratuity would be available even if the gratuity is received by the widow, children or dependents of a deceased employee.

Illustration 2 Problem on Computation of Taxable Gratuity

Mr. Ankith retires from Central Public Works Department on 30th September 2017. At the time of his retirement he receives ₹2,40,000 as Gratuity. He has rendered a total service of 33 years

9.14 • Income Tax - I

and 8 months. At the time of his retirement he was drawing basic pay ₹12,500 and DA ₹2,500. Determine the amount of exempted gratuity.

Solution:

Gratuity received at the time of retirement by a Government employee is **fully exempt** under section 10(10)(i). Mr. Ankith is a Central Government employee. Hence, Gratuity received by him is fully exempt.

Illustration 3 Problem on Computation of Taxable Gratuity

Ms. Bindu, an employee of ABC Ltd., receives ₹78,000 as Gratuity. She is covered under the Payment of Gratuity Act, 1972. She retires on 12-12-2017 after rendering service of 38 years and 8 months. At the time of retirement her basic salary and dearness allowance was ₹2,400 p.m. and ₹800 p.m. respectively. Determine the amount of exempted gratuity.

Solution:

Ms. Bindu is an employee of a company covered under the Payment of Gratuity Act, 1972. Hence exempted gratuity under section 10(10)(ii) is least of the following:

	₹
(a) $15/26 \times \text{'Last drawn Salary'} \times \text{Number of years of service.}$ [$15/26 \times ₹3,200 \times 39$]	72,000
(b) Maximum Limit	10,00,000
(c) Actual Gratuity Received	78,000

Exempted Gratuity is **₹72,000** being least of the above.

Notes:

1. Last drawn salary
= Basic Salary last drawn + DA last drawn
= ₹2,400 + ₹800
= ₹3,200
2. Number of years of service is rounded off to 39 years.

Illustration 4 Problem on Computation of Taxable Gratuity

Mr. Chethan retires on January 15, 2018 after rendering a service of 34 years and 5 months. On retirement he receives ₹1,50,000 as gratuity. At the time of retirement his monthly basic salary and dearness allowance was ₹5,000 and ₹2,000 respectively. He is covered under the Payment of Gratuity Act, 1972. Determine the amount of taxable gratuity.

Solution:

Mr. Chethan is an employee of a company covered under the Payment of Gratuity Act, 1972. Hence, taxable amount gratuity is calculated as follows:

Computation of Taxable Gratuity

	₹	₹
Actual Gratuity Received		1,50,000
Less: <i>Exempt under section 10(10)(ii), being least of the following:</i>		
(a) $15/26 \times \text{'Last drawn Salary'} \times \text{Number of years of service}$ [$15/26 \times ₹7,000 \times 35$]	1,37,308	
(b) Maximum Limit	10,00,000	
(c) Actual Gratuity Received	1,50,000	1,37,308
Taxable Gratuity		12,692

Notes:

- Last drawn salary
= Basic Salary last drawn + DA last drawn
= ₹5,000 + ₹2,000 = ₹7,000
- Number of years of service is rounded off to 34 years.

Illustration 5 Problem on Computation of Taxable Gratuity

Mr. Eshwar retires on 30-11-2017 from M/s ABC & Co., and receives ₹1,86,000 as Gratuity after rendering service of 38 years and 10 months. His salary was ₹8,000 p.m. up to 31-07-2017 and ₹9,000 p.m. from 01-08-2017. Besides, he gets ₹500 p.m. as DA (69% of which is part of salary for retirement benefits). He is not covered under the Payment of Gratuity Act, 1972. Find out the amount of Taxable Gratuity.

Solution:

Mr. Eshwar is an employee of a firm **not** covered under the Payment of Gratuity Act, 1972. Hence, the taxable gratuity is calculated using the following format:

	₹	₹
Actual Gratuity Received		1,86,000
Less: <i>Exempt under section 10(10)(iii), being least of the following:</i>		
(a) $1/2 \times \text{'Average Salary'} \times \text{Number of completed years of service.}$ [$1/2 \times ₹8,645 \times 38$]	1,64,255	
(b) Maximum Limit	10,00,000	
(c) Actual Gratuity Received	1,86,000	1,64,255
Taxable Gratuity		21,745

Notes:

1. "Salary" for Gratuity purpose

	₹
1. Basic Salary of the 10 months preceding the month of retirement (i.e., from January 2017 to October 2017 = $(8,000 \times 7) + (9,000 \times 3)$)	83,000
2. Dearness Allowance entering into retirement benefits of the 10 months preceding the month of retirement $(500 \times 10 \times 69\%)$	3,450
3. Fixed percentage commission on turnover achieved by employee of the 10 months preceding the month of retirement	Nil
Salary for gratuity purpose	86,450

$$\text{Average Salary} = ₹86,450/10 = ₹8,645$$

2. Number of completed years of service is 38.

Illustration 6 Problem on Computation of Taxable Gratuity

Mr. Fazal not being covered under the Payment of Gratuity Act, 1972 retires on 06-01-2018 from an organization and receives ₹1,24,000 as gratuity after service of 29 years & 11 months. His salary up to 30-06-2017 was ₹8,000 p.m. and thereafter it was increased by ₹500 p.m. He was entitled for DA at 35% on Basic (half of which enters for retirement benefit) and commission at 2% on turnover achieved by him. During the 10 months immediately preceding the month of retirement he achieved a turnover of ₹5,00,000. Find out the amount of Taxable Gratuity.

Solution:

Mr. Fazal is an employee of an organization not covered under the Payment of Gratuity Act, 1972. Hence taxable gratuity is calculated using the following format:

	₹	₹
Actual Gratuity Received		1,24,000
Less: <i>Exempt under section 10(10)(iii), being least of the following:</i>		
(a) $1/2 \times \text{'Average Salary'} \times \text{Number of completed years of service.}$ [$1/2 \times ₹10,787.5 \times 29$]	1,56,419	
(b) Maximum Limit	10,00,000	
(c) Actual Gratuity Received	1,24,000	1,24,000
Taxable Gratuity		Nil

Notes:

1. "Salary" for Gratuity purpose

	₹
1. Basic Salary of the 10 months preceding the month of retirement (i.e., from March 2017 to December 2017 = $(8,000 \times 4) + (8,500 \times 6)$)	83,000

	₹
2. Dearness Allowance entering into retirement benefits of the 10 months preceding the month of retirement $\{83,000 \times 35\% \times \frac{1}{2}\}$	14,875
3. Fixed percentage commission on turnover achieved by employee of the 10 months preceding the month of retirement $(5,00,000 \times 2\%)$	10,000
Salary for gratuity purpose	1,07,875

$$\text{Average Salary} = ₹1,07,875/10 = ₹10,787.50$$

2. Number of completed years of service is 29.

Illustration 7 Problem on Computation of Taxable Gratuity

Mr. Ganesh, an Accounts Manager, retired from SK Ltd., on 15/01/2018 after rendering service for 30 years 7 months. His salary is ₹25,000 per month up to 30/09/2017 and ₹27,000 thereafter. He also gets ₹2,000 per month as dearness allowance (55% of it is a part of salary for computing retirement benefits) and commission at 2.5% on turnover achieved by him. During the 10 months immediately preceding the month of retirement he achieved a turnover of ₹10,00,000. He is not covered by the Payments of Gratuity Act, 1972. He has received ₹8,00,000 as gratuity from the employer company.

Solution:

Mr. Ganesh is an employee of an organization not covered under the Payment of Gratuity Act, 1972. Hence taxable gratuity is calculated using the following format:

	₹	₹
Actual Gratuity Received		8,00,000
Less: <i>Exempt under section 10(10)(iii), being least of the following:</i>		
(a) $\frac{1}{2} \times \text{'Average Salary'} \times \text{Number of completed years of service.}$ [$\frac{1}{2} \times ₹29,200 \times 30$]	4,38,000	
(b) Maximum Limit	10,00,000	
(c) Actual Gratuity Received	8,00,000	4,38,000
Taxable Gratuity		3,62,000

Notes:

1. "Salary" for Gratuity purpose

	₹
1. Basic Salary of the 10 months preceding the month of retirement (i.e., from March 2017 to December 2017 = $(₹25,000 \times 7) + (₹27,000 \times 3)$)	2,56,000
2. Dearness Allowance entering into retirement benefits of the 10 months preceding the month of retirement $\{₹2,000 \times 10 \times 55\%\}$	11,000
3. Fixed percentage commission on turnover achieved by employee of the 10 months preceding the month of retirement $(10,00,000 \times 2.5\%)$	25,000
Salary for gratuity purpose	2,92,000

$$\text{Average Salary} = ₹2,92,000/10 = ₹29,200.$$

2. Number of completed years of service is 30.

3. Additional notes:

- Since the employee is retiring in the month of January 2018, ten preceding months are from March 2017 to December 2017.
- The Basic Salary is ₹25,000 up to 30th September, 2017 and ₹27,000 thereafter. Hence, from March to September 2017 – for a period of 7 months – it is ₹25,000 per month and from October to December 2017 – for a period of 3 months – it is ₹27,000 per month.
- Dearness Allowance must be considered only when it enters into retirement benefits. The problem clearly states that 55% of Dearness Allowance enters into retirement benefits. Hence, 55% of Dearness Allowance for the 10 months under consideration is only considered.

Illustration 8 Problem on Computation of Taxable Gratuity

Mr. Shah, an Accounts Manager, has retired from JK Ltd., on 15.01.2018 after rendering service for 30 years 7 months. His salary is ₹25,000 per month up to 30.09.2017 and ₹27,000 thereafter. He also gets ₹2000 per month as dearness allowance (55% of it is a part of salary for computing retirement benefits). He is not covered by the Payments of Gratuity Act, 1972. He has received ₹8 lakhs as gratuity from the employer company.

Solution:

In this case, assessee is **not covered** under 'The Payment of Gratuity Act'. The computation of taxable gratuity in this case is as follows:

	₹	₹
Actual Gratuity Received		8,00,000
Less: <i>Exempt under section 10(10)(iii), being least of the following:</i>		
1. $\frac{1}{2} \times \text{'Average Salary'} \times \text{Number of completed years of service. } [\frac{1}{2} \times ₹26,700 \times 30]$	4,00,500	
2. Maximum Limit	10,00,000	
3. Actual Gratuity received	8,00,000	4,00,500
Taxable Gratuity		3,99,500

Notes:

- The number of **completed** years of service = 30.
- "Average Salary" (Calculated on the basis of Salary for ten months preceding the month of retirement, i.e., March 2017 to December 2017)

	₹
Basic Salary $[(₹25,000 \times 7) + (₹27,000 \times 3)]$	2,56,000
Dearness Allowance $(₹2,000 \times 10 \times 55/100)$	11,000
	2,67,000

'Average Salary' = ₹2,67,000/10 = ₹26,700.

Notes:

- Since the employee is retiring in the month of January 2018, ten preceding months are from March 2017 to December 2017.
- The Basic Salary is ₹25,000 up to 30th September, 2017 and ₹27,000 thereafter. Hence, from March to September 2017 – for a period of 7 months – it is ₹25,000 per month and from October to December 2017 – for a period of 3 months – it is ₹27,000 per month.
- Dearness Allowance must be considered only when it enters into retirement benefits. The problem clearly states that 55% of Dearness Allowance enters into retirement benefits. Hence, 55% of Dearness Allowance for the 10 months under consideration is only considered.

Illustration 9 Problem on Computation of Taxable Gratuity

Mr. Q, who served for 28 years and 8 months with his employer, retired from services on the 31st of December, 2017. At the time of his retirement, his basic salary was ₹50,000 per month (which was ₹46,250 per month up to July, 2017). He was also entitled for a dearness allowance of 40% (75% of which entered into retirement benefits), other taxable allowances of ₹15,000 per month and a commission on sales achieved by him @ 2.5%. (During calendar year 2017, his average monthly sales were ₹75,000). In September, 2017 he was given a commission on profits of ₹50,000.

On his retirement, he received a gratuity of ₹14,00,000. Mr. Q was earlier working on a part-time job, which fetched him a gratuity of ₹1,00,000 (this gratuity was fully exempt).

Compute the taxable gratuity of Mr. Q for the assessment year 2018-19, if he was

- a secretary in the Finance Department of Karnataka Government;
- an employee of MRF Ltd., which was covered under the Factories Act; and
- an employee of a private company at Bangalore.

Solution:

Case (a):

Gratuity received at the time of retirement by a Government employee is **fully exempt** under section 10(10)(i).

Case (b):

In this case, the assessee was an employee of a company **covered** under the Factories Act. Hence, he is covered under the 'The Payment of Gratuity Act'. The computation of taxable gratuity in this case, is as follows:

	₹	₹
Actual Gratuity Received		14,00,000
Less: Exempt under section 10(10)(ii), being least of the following:		

9.20 • Income Tax - I

	₹	₹
(a) $15/26 \times \text{'Last drawn Salary'} \times \text{Number of years of service}$ a. $[15/26 \times ₹70,000 \times 29]$	11,71,154	
(b) Maximum Limit (₹10,00,000 <i>less</i> ₹1,00,000)	9,00,000	
(c) Actual Gratuity Received	14,00,000	9,00,000
Taxable Gratuity		5,00,000

Notes:

- Number of years of service = 29 (rounded off).
- 'Last Drawn Salary' (Calculated on the basis of salary for last month of service, i.e., December 2017)*

Basic Salary	₹50,000
Dearness Allowance (40% of ₹50,000)	₹20,000
	<u>₹70,000</u>

Note: There is no condition to be fulfilled for considering Dearness Allowance in calculation of 'Last Drawn Salary', when the employee is covered under the Payment of Gratuity Act.

- Since, the assessee had earlier claimed an exemption of ₹1,00,000 towards gratuity, the maximum exemption is now restricted to ₹9,00,000.

Case (c):

In this case, assessee is an employee of a commercial office and hence he is **not covered** under 'The Payment of Gratuity Act'. The computation of taxable gratuity in this case is as follows:

	₹	₹
Actual Gratuity received		14,00,000
Less: Exempt under section 10(10)(iii), being least of the following:		
(a) $1/2 \times \text{'Average Salary'} \times \text{Number of completed years of service. } [1/2 \times ₹63,950 \times 28]$	8,95,300	
(b) Maximum Limit [₹10,00,000 <i>less</i> ₹1,00,000]	9,00,000	
(c) Actual Gratuity received	14,00,000	8,95,300
Taxable Gratuity		5,04,700

Notes:

- Number of **Completed** years of service = 28.
- "Average Salary" (Calculated on the basis of Salary for ten months preceding the month of retirement, i.e., February 2017 to November 2017)*

	₹
(a) Basic Salary [$(₹46,250 \times 6) + (₹50,000 \times 4)$]	4,77,500
(b) Dearness Allowance $(₹4,77,500 \times 40/100 \times 75/100)$	1,43,250
(c) Commission based on fixed percentage of turnover achieved by employee $(₹75,000 \times 10 \times 2.5/100)$	18,750
	6,39,500

'Average Salary' = $₹6,39,500/10 = ₹63,950$.

Notes:

- Since the employee is retiring in the month of December 2017, ten preceding months are from February 2017 to November 2017.
 - The Basic Salary is ₹46,250 up to 31st July 2017 and ₹50,000 thereafter. Hence, from February to July 2017 – for a period of 6 months – it is ₹46,250 per month and from August to November 2017 – for a period of 4 months – it is ₹50,000 per month.
 - Dearness Allowance must be considered only when it enters into retirement benefits. The problem clearly states that 75% of Dearness Allowance enters into retirement benefits. Hence, 75% of Dearness Allowance for the 10 months under consideration is only considered. The amount of Dearness Allowance is 40%, which represents 40% of Basic Salary.
 - Commission on profits must not be included. Only commission on sales achieved by employee during the relevant 10 months, calculated as a percentage, must only be considered. In this case, the average sales per month are ₹75,000. Accordingly, the commission on sales has been calculated.
- Since, the assessee had earlier claimed an exemption of ₹1,00,000 towards gratuity, the maximum exemption is now restricted to ₹9,00,000.

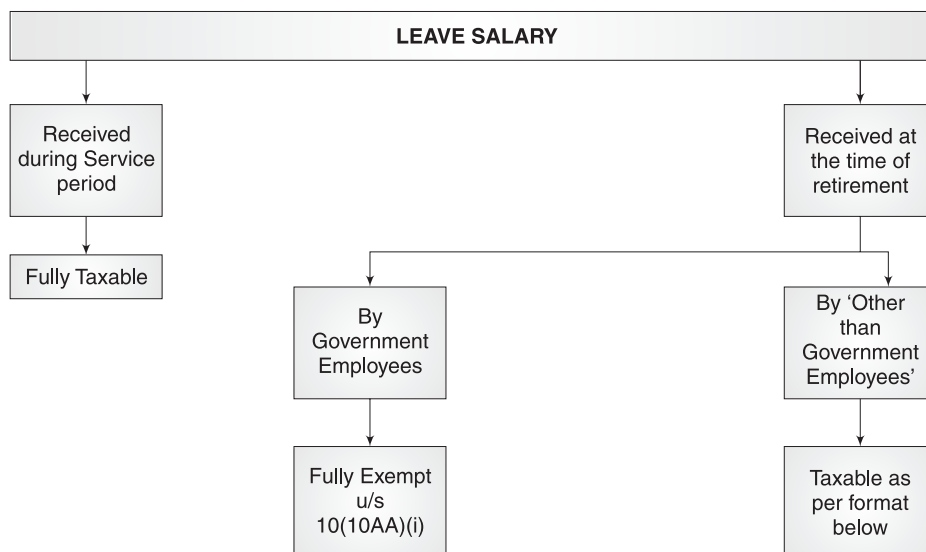
9.6.9 Leave Salary or Salary in Lieu of Leave or Encashment of Earned Leave

'Leave Salary' refers to salary paid to employee for 'earned leave' facility not availed by him. Earned Leave is a leave facility made available to an employee. It is the period of leave sanctioned to employee, in accordance with company's policy, in addition to casual leave. It is the period of leave for which the assessee earns salary, and when it is not availed (fully or partly), he gets additional salary for the period of earned leave not availed by him and such additional salary is called 'leave salary'.

While casual leave not availed by an employee cannot be carried forward to the next period, the earned leave not availed by an employee during a given period, can be carried forward to the next period. Further, the casual leave not availed cannot be encashed, but earned leave not availed can be encashed – either during service period or at the time of retirement.

When an employee encashes his earned leave not availed, the tax treatment for the amount received by him is summarised in the following chart:

9.22 • Income Tax - I



Format for computing Taxable Leave Salary received at the time of retirement by 'Other than Government Employee'

	₹	₹
Actual Leave Salary Received		XXX
Less: <i>Exempt under section 10(10AA)(ii), being least of the following:</i>		
(a) Leave at the credit of employee × "Average Salary"	XXX	
(b) 10 Months' "Average Salary"	XXX	
(c) Maximum Limit	3,00,000	
(d) Actual Leave Salary Received	XXX	XXX
Taxable Leave Salary		XXX

Notes:

1. Leave at the credit of employee = Leave entitlement *minus* leave availed.
2. According to the provisions under the Income Tax Act, Leave entitlement = Actual leave entitled by employer per annum or 1 month (30 days) per annum, whichever is less – for every **completed** year of service.
3. For example, suppose an employee has rendered 30 completed years of service with his employer, till his retirement. Also suppose that as per company's policy the leave entitled was 45 days (1.5 month) for each year of completed service. Then, 'Leave Entitlement' will be – 1.5 months or 1 month, whichever is less – 1 month, for each completed year of service – that is, 1 month × 30 years = 30 months. In the same example, if the leave entitled by the employer was 20 days for each year of completed service. Then, 'Leave Entitlement' will be – 20 days or 30 days, whichever is less – 20 days for each completed

year of service – that is, 20 days \times 30 years = 600 days (i.e., 20 months – 600 days/30 days).

4. Where, leave availed exceeds 'Leave Entitlement', the 'leave at the credit of employee' must be considered as 'Nil'.
5. 'Average Salary' refers to **Total** of Basic Salary, Dearness Pay, Dearness Allowance (if it enters into retirement benefits) and Commission based on a fixed percentage of turnover achieved by employee for 10 months preceding the *date* of retirement of the employee, **divided by 10**.
6. For example, where an employee retires from his services on 15th of December, 2017 – ten months preceding the *date* of retirement would be – 16th February 2017 to 15th December 2017.
7. The maximum exemption of ₹3,00,000 is for the life-time of the assessee and not for each time exemption is claimed. Where the assessee had earlier received any leave salary and such leave salary was exempt partly or fully, and when exemption is being calculated for leave salary received next time, the maximum exemption will be ₹3,00,000 **as reduced by** the amount of leave salary exempted earlier.
8. Where 'leave at the credit of the employee' is 'Nil', then, there is no exemption available under section 10(10AA)(ii). That is, the entire amount of leave salary received would become taxable.

Illustration 10 Problem on Computation of Taxable Leave Salary

Mr. Akhil retires from Central Public Works Department on 30th September 2017. At the time of his retirement he receives ₹2,40,000 as Leave Encashment. He has rendered a total service of 33 years and 8 months. At the time of his retirement he was drawing basic pay ₹12,500 and Dearness Allowance of ₹2,500. Determine the amount of exempted leave encashment.

Solution:

Leave encashment received at the time of retirement by a Government employee is **fully exempt** under section 10(10AA)(i). Mr. Akhil is a Central Government employee. Hence, leave encashment received by him is fully exempt.

Illustration 11 Problem on Computation of Taxable Leave Salary

Mr. Bhaskar receives ₹4,20,000 as leave encashment at the time of his retirement on 30-11-2017. Determine the amount of taxable leave encashment from the following information: Salary up to 30-06-2017 ₹20,500 per month and thereafter ₹21,000 per month. Duration of service 26 years and 8 months; Leave availed while in service 6 months; Leave entitlement is one month for every completed year of service.

Solution:

Mr. Bhaskar is not a Government Employee. Hence, taxable amount of leave encashment is calculated as follows:

Computation of Taxable Leave Encashment

	₹	₹
Actual Leave Encashment Received		4,20,000
Less: <i>Exempt under section 10(10AA)(ii), being least of the following:</i>		
• Leave at the credit of employee × “Average Salary” [20 × ₹20,750]	4,15,000	
• 10 Months’ “Average Salary” [10 × ₹20,750]	2,07,500	
• Maximum Limit	3,00,000	
• Actual Leave Salary Received	4,20,000	2,07,500
Taxable Leave Salary		2,12,500

Notes:

- For tax purposes, the leave at the credit of employee must be calculated as follows:
 - Number of completed years of service = 26
 - Leave entitlement – One month for every completed year of service = 26 months.
 - Leave availed by employee during service period = 6 months.
 - Leave at the credit of employee
 = Leave entitlement minus leave availed while in service
 = 26 months – 6 months
 = 20 months.
- “Salary” for Leave Encashment purpose

	₹
1. Basic Salary of the 10 months preceding the date of retirement (i.e., from February 2017 to November 2017 = $(20,500 \times 5) + (21,000 \times 5)$)	2,07,500
2. Dearness Allowance entering into retirement benefits of the 10 months preceding the date of retirement	Nil
3. Fixed percentage commission on turnover achieved by employee of the 10 months preceding the date of retirement	Nil
Salary for leave encashment purpose	2,07,500

$$\text{Average Salary} = ₹2,07,500/10 = ₹20,750.$$

Illustration 12 Problem on Computation of Taxable Leave Salary

Mr. Chandru receives ₹10,32,000 as leave encashment at the time of his retirement on 31-12-2017. Determine the amount of taxable leave encashment from the following information: Salary up to 31-7-2017 ₹22,000 p.m; Salary from 01-08-2017 ₹24,000 p.m; Duration of service 34 years; Leave availed while in service 8 months; Leave at credit of Mr. B at the time of his retirement as per company records 43 months.

Solution:

Mr. Chandru is not a Government Employee. Hence, taxable amount of leave encashment is calculated as follows:

Computation of Taxable Leave Encashment

	₹	₹
Actual Leave Encashment Received		10,32,000
Less: <i>Exempt under section 10(10AA)(ii), being least of the following:</i>		
(a) Leave at the credit of employee × “Average Salary” [26 × ₹23,000]	5,98,000	
(b) 10 Months’ “Average Salary” [10 × ₹23,000]	2,30,000	
(c) Maximum Limit	3,00,000	
(d) Actual Leave Salary Received	10,32,000	2,30,000
Taxable Leave Salary		8,02,000

Notes:

- For tax purposes, the leave at the credit of employee must be calculated as follows:
 - Number of Completed years of service = 34
 - Leave entitlement as per company records is 51 months (as per company records leave availed is 8 months and leave at credit is 43 months. Hence, leave entitlement as per company policy is 51 months (i.e., 8 + 43). However, for income tax purpose, leave entitlement shall be restricted to one month for every completed year of service. Therefore, leave entitlement should be taken as 34 months.
 - Leave availed by employee during service period = 6 months.
 - Leave at the credit of employee
 = Leave entitlement minus leave availed while in service
 = 34 months – 8 months
 = 26 months
- “Salary” for Leave Encashment purpose

	₹
(i) Basic Salary of the 10 months preceding the date of retirement (i.e., from March 2017 to December 2017 = (22,000 × 5) + (24,000 × 5)	2,30,000
(ii) Dearness Allowance entering into retirement benefits of the 10 months preceding the date of retirement	Nil
(iii) Fixed percentage commission on turnover achieved by employee of the 10 months preceding the date of retirement	Nil
Salary for leave encashment purpose	2,30,000

$$\text{Average Salary} = ₹2,30,000/10 = ₹23,000.$$

Illustration 13 Problem on Computation of Taxable Leave Salary

Mr. Dhananjay receives ₹3,80,000 as leave encashment at the time of his retirement on 28-02-2018. Determine the amount of taxable leave encashment from the following information: Basic Salary up to 30-6-2017 ₹8,000 p.m and thereafter ₹9,500 pm; Duration of service 36 years and 9 months; Leave entitlement as per company rules – 2 months for every year of service; Leave at credit of Mr. D at the time of retirement as per company records 40 months.

Solution:

Mr. Dhananjay is not a Government Employee. Hence, taxable amount of leave encashment is calculated as follows:

Computation of Taxable Leave Encashment

	₹	₹
Actual Leave Encashment received		3,80,000
Less: <i>Exempt under section 10(10AA)(ii), being least of the following:</i>		
(a) Leave at the credit of employee × “Average Salary” [4 × ₹8,750]	35,000	
(b) 10 Months’ “Average Salary” [10 × ₹8,750]	87,500	
(c) Maximum Limit	3,00,000	
(d) Actual Leave Salary received	3,80,000	35,000
Taxable Leave Salary		3,45,000

Notes:

1. For tax purposes, the leave at the credit of employee must be calculated as follows:

- (a) Number of Completed years of service = 36
- (b) Leave entitlement as per company records is 72 months. However, for income tax purpose, leave entitlement shall be restricted to one month for every completed year of service. Therefore, leave entitlement should be taken as 36 months.
- (c) Leave availed by employee during service period – 32 months. This is calculated as follows:
 Leave at credit as per company records = Leave entitlement as per company records
 – Leave availed while in service as per company records
 i.e., 40 = 72 – Leave availed
 Leave availed = 72 – 40 = 32
- (d) Leave at the credit of employee for income tax purpose
 = Leave entitlement – Leave availed while in service
 = 36 months – 32 months
 = 4 months.

2. “Salary” for Leave Encashment purpose

	₹
(i) Basic Salary of the 10 months preceding the date of retirement (i.e., from May 2017 to February 2018 = $(8,000 \times 5) + (9,500 \times 5)$)	87,500
(ii) Dearness Allowance entering into retirement benefits of the 10 months preceding the date of retirement	Nil
(iii) Fixed percentage commission on turnover achieved by employee of the 10 months preceding the date of retirement	Nil
Salary for leave encashment purpose	87,500

Average Salary = ₹87,500/10 = ₹8,750.

Illustration 14 Problem on Computation of Taxable Leave Salary

Mr. Venkatesh was employed by PQR Ltd., up to 15-03-1991. At the time of leaving the job at PQR Ltd., he was paid ₹3,50,000 as leave salary out of which ₹87,000 was exempt from tax u/s 10. Thereafter he joined LMN Ltd., and received ₹7,59,000 as leave salary at the time of his retirement on 31-12-2017 from this company.

Determine the amount of taxable leave salary from the following information: Salary at the time of retirement ₹23,000 p.m. Average salary received during the 10 months ending on 31-12-2017: From 1-03-2017 to 31-07-2017 ₹22,600 p.m. and from 1-08-2017 to 31-12-2017 ₹23,000 p.m. Duration of service 24 years 9 months.

Leave entitlement 1½ months for every completed year of service. Leave availed while in service 3 months.

Solution:

Mr. Venkatesh is not a Government Employee. Hence, taxable amount of leave encashment is calculated as follows:

Computation of Taxable Leave Encashment

	₹	₹
Actual Leave Encashment received		7,59,000
Less: <i>Exempt under section 10(10AA)(ii), being least of the following:</i>		
(a) Leave at the credit of employee × “Average Salary” [21 × ₹22,800]	4,78,800	
(b) 10 Months’ “Average Salary” [10 × ₹22,800]	2,28,000	
(c) Maximum Limit (3,00,000 – 87,000)	2,13,000	
(d) Actual Leave Salary received	3,80,000	2,13,000
Taxable Leave Salary		5,46,000

Notes:

1. For tax purposes, the leave at the credit of employee must be calculated as follows:
 - (a) Number of Completed years of service = 24
 - (b) Leave entitlement as per company records is 36 months (i.e., 24×1.5 months). However, for income tax purpose, leave entitlement shall be restricted to one month for every completed year of service. Therefore, leave entitlement should be taken as 24 months.
 - (c) Leave availed by employee during service period = 3 months.
 - (d) Leave at the credit of employee for income tax purpose
 = Leave entitlement – Leave availed while in service
 = 24 months – 3 months
 = 21 months.
 - (e) Since, the assessee had earlier claimed an exemption of ₹87,000 towards leave salary, the maximum exemption is now restricted to ₹2,13,000.
2. “Salary” for Leave Encashment purpose

	₹
(i) Basic Salary of the 10 months preceding the date of retirement (i.e., from March 2017 to December 2017 = $(22,600 \times 5) + (23,000 \times 5)$)	2,28,000
(ii) Dearness Allowance entering into retirement benefits of the 10 months preceding the date of retirement	Nil
(iii) Fixed percentage commission on turnover achieved by employee of the 10 months preceding the date of retirement	Nil
Salary for leave encashment purpose	2,28,000

Average Salary = ₹2,28,000/10 = ₹22,800.

Illustration 15 Problem on Computation of Taxable Leave Salary

Suraj was employed by PQR Ltd., up to March 15, 1993. At the time of leaving PQR Ltd., he was paid ₹3,50,000 as leave salary out of which ₹57,000 was exempt from tax. Thereafter he joined the present employer and received ₹4,14,000 as leave salary at the time of his retirement on December 31, 2017. Determine the amount of taxable leave salary from the following information, when the present employer is—

- (a) The Government of Kerala,
- (b) Bata Ltd.

Salary at the time of retirement – ₹23,000 per month.

Salary up to June 2017 – ₹20,000 per month.

Dearness Allowance – 20% of Basic Salary (25% of which enters into retirement benefits)

Duration of Service – 23 years, 9 months and 15 days.

Leave entitlement for every year of service – 45 days

Leave availed while in service – 450 days

Leave at the credit of employee at the time of retirement – 19.5 months.

Solution:

Case (a):

Leave salary received by a Government employee at the time of retirement is *fully exempt* under section 10(10AA)(i)

Case (b):

Computation of Taxable amount of Leave Salary received at the time of retirement, by 'other than Government Employee' is as shown below:

	₹	₹
Actual Leave Salary received		4,14,000
Less: <i>Exempt under section 10(10AA)(ii), being least of the following:</i>		
(a) Leave at the credit of employee × "Average Salary" [8 × ₹22,890]	1,83,120	
(b) 10 Months' "Average Salary" [10 × ₹22,890]	2,28,900	
(c) Maximum Limit (₹3,00,000 <i>minus</i> ₹57,000)	2,43,000	
(d) Actual Leave Salary received	4,14,000	1,83,120
Taxable Leave Salary		2,30,880

Notes:

1. Leave at the credit of employee given in the problem is calculated on the basis of employer's leave entitlement. This must not be considered for tax purposes.
2. For tax purposes, the leave at the credit of employee must be calculated as follows:
 - Number of Completed years of service = 23
 - Leave entitlement – 45 days (entitled by employer) **or** 30 days (limit as per Income Tax Provisions), whichever is less, for each completed year of service. So, 'Leave Entitlement' is 690 days (i.e., 30 days × 23 years).
 - Leave availed by employee during service period is 450 days.
 - Leave at the credit of employee = 690 days *minus* 450 days = **240 days or 8 months** (i.e., 240 days/30 days).
3. "Average Salary" (Calculated on the basis of Salary for ten months preceding the date of retirement, i.e., March 2017 to December 2017)

	₹
Basic Salary [(₹20,000 × 4) + (₹23,000 × 6)]	2,18,000
Dearness Allowance (₹2,18,000 × 20/100 × 25/100)	10,900
	2,28,900

‘Average Salary’ = ₹2,28,900/10 = ₹22,890.

Notes:

- (a) Since the employee is retiring on 31st December 2017, ten months preceding the date of retirement are from March 2016 to December 2016.
 - (b) The Basic Salary is ₹20,000 up to 30th June, 2017 and ₹23,000 thereafter. Hence, from March to June 2017 – for a period of 4 months – it is ₹20,000 per month and from July to December 2017 – for a period of 6 months – it is ₹23,000 per month.
 - (c) Dearness Allowance must be considered only when it enters into retirement benefits. The problem clearly states that 25% of Dearness Allowance enters into retirement benefits. Hence, 25% of Dearness Allowance for the 10 months under consideration is only considered. The amount of Dearness Allowance is 20% of Basic Salary for the relevant ten months.
4. Since, the assessee had earlier claimed an exemption of ₹57,000 towards leave salary, the maximum exemption is now restricted to ₹2,43,000.

9.6.10 Pension

The provisions relating to ‘pension’ has been classified into the following:

- A. Contribution made by Employer to the Notified Pension Fund Scheme of Central Government (i.e., National Pension Scheme) in the name of employee, who has joined services on or after 1st January, 2004.
- B. Regular or Normal Pension received by employee after termination of employment.
- C. Commuted Pension.

A. Contribution made by Employer to the Notified Pension Fund Scheme of Central Government (i.e., National Pension Scheme) in the name of employee, who has joined Central Government services on or after 1st January, 2004.

For assessee joining the services of Central Government on or after 1st January, 2004, pension benefit from employer was not made available. Instead, the employees were made members of the National Pension Scheme of the Central Government to which the employee was made to contribute (by effecting deduction from his salary) and a further contribution was also made by employer (i.e., Central Government). On retirement, the employee gets pension from the National Pension Scheme.

This benefit of National Pension Scheme was later extended to other employees as well.

Where employer (being Central Government or any other employer) contributes to the National Pension Scheme in the name of the employee, it is a benefit passing from employer to employee and hence is an income from salary.

The **contribution made by employer** is **completely taxable** under the head “Income from Salaries”. However, for the contribution made by both employer and employee, a deduction can be claimed under section 80CCD, from Gross Total Income.

B. Regular or Normal Pension received by employee after termination of employment.

Any pension received by assessee, in regular intervals, after termination of service is **completely taxable** in the hands of the assessee as 'Income from Salary', irrespective of whether the assessee was a Government employee or 'Other than Government' employee. Since, the payment of pension is based on 'employer-employee' relationship and the payment is 'based on employment', pension is taxable under the head 'income from salary'.

The Regular Pension or Normal Pension or Un-commuted Pension is taxable on '**accrual**' or '**receipt**' basis, whichever happens earlier.

C. Commuted Pension

'Commuted Pension' refers to 'pension received in advance'. It represents lump-sum amount received **in lieu of** entire or part of pension to be received in future.

Pension being taxable on 'accrual' or 'receipt' basis, whichever happens first, Commuted Pension is **taxable in the year of receipt**.

Section 10(10A) of the Income Tax Act, 1961 gives the provisions for tax treatment of commuted pension, The tax treatment for this receipt depends on the following situations:

- Pension commuted by an assessee who was a Government Employee or Semi-Government Employee.
- Pension commuted by an assessee who was a 'Non-Government Employee' and had received gratuity from employer either during service period or at the time of retirement.
- Pension commuted by an assessee who was a 'Non-Government Employee' and had not received any gratuity from his employer.

The tax treatment for commuted pension under each of the above situations, is explained below:

- Pension commuted by an assessee who was a Government Employee or Semi-Government Employee.*

The lump-sum amount received, on commutation of entire or part amount of future pension, by an assessee who was a Government Employee or Semi-Government Employee is **fully exempt** under section 10(10A)(i)

- Pension commuted by an assessee who was a '**Non-Government Employee**' and **had received gratuity** from employer either during service period or at the time of retirement.*

In this case, the following format is used for computing taxable amount of commuted pension:

	₹
Commuted Value of Pension (i.e., lump sum amount received)	XXX
Less: Exempt under section 10(10A)(ii) – 1/3 X 'Actual Value of Commuted Pension'	XXX
Taxable Commuted Pension	XXX

(c) *Pension commuted by an assessee who was a 'Non-Government Employee' and had not received any gratuity from his employer.*

In this case, the following format is used for computing taxable amount of commuted pension:

	₹
Commuted Value of Pension (i.e., lump sum amount received)	XXX
Less: Exempt under section 10(10A)(ii) – 1/2 X 'Actual Value of Commuted Pension'	XXX
Taxable Commuted Pension	XXX

Note:

'Actual Value of Commuted Pension' refers to the pension which the retired employee is normally entitled to receive. It is calculated in the following manner:

$$\text{Lump-sum amount received} \times (\text{Actual Pension/Commuted Portion of Pension})$$

For example, suppose an employee was receiving ₹ 10,000 per month as pension, after his retirement. In the month of April 2017, he commutes 70% of his pension for a lump-sum of ₹ 3,15,000.

That is, from the month of April 2017, his normal pension will be ₹ 3,000 per month (i.e., 30% of ₹ 10,000), which is also called 'un-commuted pension'. For previous year 2017-18, the total amount of 'normal' or 'un-commuted' pension is ₹ 36,000 (₹ 3,000 × 12).

The commuted portion of pension (in lieu of which he is getting a lump-sum of ₹ 3,15,000) is ₹ 7,000 (i.e., 70% of ₹ 10,000). So, the **'Actual Value of Commuted Pension'** is – (₹ 3,15,000 × ₹ 10,000/₹ 7,000) = ₹ 4,50,000.

In the above example, suppose the commutation of pension is made in the month of November 2017, then the amount of 'normal' or 'un-commuted' pension for previous year 2017-18 will be – (₹ 10,000 × 7) + (₹ 3,000 × 5) = ₹ 85,000 [That is, ₹ 10,000 per month up to October 2017, and ₹ 3,000 per month from November 2017].

Illustration 16 Problem on computation of Taxable Pension

Mr. Amit receives ₹ 15,000 p.m. as pension from Central Government during the Previous Year 2017-18. What is the taxable pension for the Assessment Year 2018-19?

Solution:

Regular or normal pension received is fully taxable in case of all employees. Hence, the taxable pension in this case is ₹ 1,80,000 (i.e., ₹ 15,000 × 12).

Illustration 17 Problem on computation of Taxable Pension

Mr. Balaji receives ₹ 20,000 p.m. as pension from ABC Ltd., during the Previous Year 2017-18. What is the taxable amount of pension for the Assessment Year 2018-19?

Solution:

Regular or normal pension is fully taxable in case of all employees. Hence, the taxable pension in this case is ₹2,40,000 (i.e., ₹20,000 × 12).

Illustration 18 Problem on computation of Taxable Pension

Ms. Chandrakala retires from ABC Ltd. on 31-08-2017. On his retirement pension is fixed at ₹30,000 p.m. What is the taxable amount of pension for the Assessment Year 2018-19?

Solution:

Regular or normal pension is fully taxable in case of all employees. Ms. Chandrakala has retired from service on 31-08-2017 and starts getting pension from the month of September 2017. She receives pension for 7 months from September 2017 to March 2018. Hence, the taxable pension is ₹2,10,000 (i.e., ₹20,000 × 7).

Illustration 19 Problem on computation of Taxable Pension

Mr. Dheemanth was receiving ₹16,000 p.m. as pension. On 1-8-2017 he commutes ₹4,000 of his pension for a lump sum of ₹4,80,000. Calculate Actual Value of Commuted Pension.

Solution:

Actual Value of Commuted Pension

$$\begin{aligned}
 &= \text{Lump-sum amount received} \times (\text{Actual Pension/Commuted Portion of Pension}) \\
 &= 4,80,000 \times (16,000/4,000) \\
 &= ₹19,20,000.
 \end{aligned}$$

Illustration 20 Problem on computation of Taxable Pension

Mr. Edwin commutes 35% of his pension for ₹1,40,000. Calculate Actual Value of Commuted Pension.

Solution:

Actual Value of Commuted Pension

$$\begin{aligned}
 &= \text{Lump-sum amount received} \times (\text{Actual Pension/Commuted Portion of Pension}) \\
 &= 1,40,000 \times (100/35) \\
 &= ₹4,00,000
 \end{aligned}$$

Illustration 21 Problem on computation of Taxable Pension

Mr. Fazal commutes 1/3 of his pension for ₹1,50,000. Find out the Actual Value of Commuted Pension.

Solution:

Actual Value of Commuted Pension or Commutation Value of Full Pension

$$\begin{aligned}
 &= \text{Lump-sum amount received} \times (\text{Actual Pension/Commuted Portion of Pension}) \\
 &= 1,50,000 \times (3/1) \\
 &= ₹4,50,000.
 \end{aligned}$$

Illustration 22 Problem on computation of Taxable Pension

Mr. Girish retires from the Central Government employment on May 31, 2017. He gets pension of ₹25,000 p.m. up to 30-11-2017. With effect from 1-12-2017 he gets 40% of his pension commuted for ₹10,00,000. Determine the amount of taxable pension for the AY 2018-19.

Solution:

As Mr. Girish was a **Government employee** and has commuted his pension during the Previous Year 2017-18, the following calculations are necessary for calculating taxable pension

Regular/Normal/Un-commuted Pension – Since, 40% of the regular pension is commuted in the month of November, 2017 the un-commuted pension up-to November, 2017 will be ₹25,000 per month and thereafter i.e., from December 2017 it will be ₹15,000 (i.e., 60% of ₹25,000) per month.

So, the total un-commuted pension is: $(25,000 \times 6) + (15,000 \times 4) = \text{₹}2,10,000$.

Computation of taxable pension

	₹	₹
Regular/Normal/Un-commuted Pension		2,10,000
Commuted Pension	10,00,000	
Less: Exempt under section 10(10A)(i)	10,00,000	Nil
Taxable Pension		2,10,000

Note: Since Mr. Girish is Central Government employee, the entire amount of commuted value of pension is exempted under section 10(10A)(i).

Illustration 23 Problem on computation of Taxable Pension

Mr. Hemanth retires from PQR Ltd., on 31-03-2017. He gets ₹14,000 p.m. as pension but does not receive any gratuity. On his request PQR Ltd. pays ₹3,00,000 in lieu of commutation of 40% of pension with effect from 01-02-2018. Determine the amount of taxable pension.

Solution:

As Mr. Hemanth is **not a Government employee and is not in receipt** of gratuity and has commuted his pension during the Previous Year 2017-18, the following calculations become necessary for calculating taxable pension:

- 1. Regular/Normal/Un-commuted Pension** – Since, 40% of the regular pension is commuted with effect from 01-02-2018 the un-commuted pension up-to January, 2017 will be ₹14,000 per month and thereafter i.e., from February 2017 it will be ₹8,400 (i.e., 60% of ₹14,000) per month.

So, the total un-commuted pension is $(\text{₹}14,000 \times 10) + (\text{₹}8,400 \times 2) = \text{₹}1,56,800$

- 2. Actual Value of Commuted Pension'**

$$\begin{aligned}
 &= \text{Lump-sum amount received} \times (\text{Actual Pension/Commuted Portion of Pension}) \\
 &= 3,00,000 \times (100/40) \\
 &= \text{₹}5,00,000.
 \end{aligned}$$

Computation of taxable pension

	₹	₹
Regular/Normal/Un-commuted Pension		1,56,800
Commuted Pension	3,00,000	
Less: Exempt under section 10(10A)(i) (1/2 of ₹5,00,000)	2,50,000	50,000
Taxable Pension		2,06,800

Notes: Since Mr. Hemanth is not a Government employee and not receiving any gratuity, ½ of Actual Value of Commuted Pension is exempt under section 10(10A)(i).

Illustration 24 Problem on computation of Taxable Pension

Ms. Indrani retires from LMN Ltd., on 30-06-2017. She gets pension of ₹20,000 p.m. up to 31-01-2018. With effect from 01-02-2018 she gets 60% of pension commuted for ₹4,00,000. Determine the taxable pension if Mr. Indrani had received gratuity at the time of retirement.

Solution:

Ms. Indrani was a **Non-Government employee who was in receipt** of gratuity, She has commuted her pension during the Previous Year 2017-18. For calculating taxable pension, the following calculations are necessary:

- 1. Regular/Normal/Un-commuted Pension** – Since, 60% of the regular pension is commuted with effect from 01-02-2018 the un-commuted pension up-to January, 2018 will be ₹20,000 per month and thereafter i.e., from February 2018 onwards it will be ₹8,000 (i.e., 40% of ₹20,000) per month.

So, total un-commuted pension is $(₹20,000 \times 7) + (₹8,000 \times 2) = ₹1,56,000$.

- 2. Actual Value of Commuted Pension' or Commutation Value of Full Pension**
 = Lump-sum amount received \times (Actual Pension/Commuted Portion of Pension)
 = $4,00,000 \times (100/60)$
 = ₹6,66,667.

Computation of taxable pension

	₹	₹
Regular/Normal/Un-commuted Pension		1,56,000
Commuted Pension	4,00,000	
Less: Exempt under section 10(10A)(i) (1/3 of ₹6,66,667)	2,22,222	1,77,778
Taxable Pension		3,33,778

Notes: Since Ms. Indrani is not a Government employee and is in receipt of gratuity, 1/3 of Actual Value of Commuted Pension is exempted under section 10(10A)(i).

Illustration 25 Problem on computation of Taxable Pension

Mr. Jayaram, who retired from his services in 2009, has been receiving a monthly pension of ₹5,000, from the date of his retirement. On 13th August, 2017 he commuted 70% of his pension

9.36 • Income Tax-I

for a lump sum consideration of ₹52,500. Compute his taxable pension for the previous years 2016-17, 2017-18, and 2018-19, if he was

- (i) an employee of P&T Department;
- (ii) an employee of Reliable Ltd., who had received ₹3,00,000 as gratuity at the time of his retirement; and
- (iii) an employee of Tata Sons Ltd., who had not received any gratuity.

Solution:

For Previous Year 2016 – 17 (Assessment Year 2017-18)

Taxable Pension = ₹60,000 (₹5,000 × 12), in all cases.

For Previous Year 2017 – 18 (Assessment Year 2018-19)

During this previous year, assessee has commuted pension. Hence, for calculating taxable pension the following must be ascertained:

- (i) Actual Pension per month – ₹5000.
- (ii) Commuted Portion of Pension – 70% – ₹3,500 per month.
- (iii) Commuted Value of Pension (lump-sum received) – ₹52,500.
- (iv) Actual Value of Commuted Pension – (₹52,500 × ₹5,000/₹3,500) = ₹75,000.
- (v) Un-commuted Pension or Normal Pension

₹5,000 per month up to July 2017 and ₹1,500 (30% of ₹5,000) per month from August 2017 onwards.

So, un-commuted pension for previous year 2017-18 is (₹5,000 × 4) + (₹1,500 × 8) = ₹32,000.

Case (i) – When Assessee was an employee of P&T Department:

	₹	₹
Normal or Un-commuted Pension		32,000
Commuted Pension	52,500	
Less: Exempt under section 10(10A)(i)	52,500	Nil
Taxable Pension		32,000

Case (ii) – When Assessee was an employee of Reliable Ltd., who had received ₹3,00,000 as gratuity at the time of his retirement

	₹	₹
Normal or Un-commuted Pension		32,000
Commuted Pension	52,500	
Less: Exempt under section 10(10A)(ii) –		
One-third of 'Actual Value of Commuted Pension (1/3 × ₹75,000)	25,000	27,500
Taxable Pension		59,500

Case (iii) – When Assessee was an employee of Tata Sons Ltd., who had not received any gratuity

	₹	₹
Normal or Un-commuted Pension		32,000
Commuted Pension	52,500	
Less: Exempt under section 10(10A)(ii)–		
Two-third of 'Actual Value of Commuted Pension ($1/2 \times ₹75,000$)	37,500	15,000
Taxable Pension		47,000

For and From Previous Year 2018-19 (From Assessment Year 2019-20 and onwards)

Taxable Pension = ₹18,000 (₹1,500 × 12) in all cases

ALLOWANCES UNDER SECTION 17(3)

9.7

An 'allowance' is a regular, fixed, monetary payment made by employer to employee to enable the employee to render his services in a comfortable manner.

The purpose of the allowance is to either help or assist the employee in his performance of official duties or for meeting his personal expenses.

For considering any benefit given by employer to employee as an **allowance**, the following three criteria must be fulfilled:

- Regularity – the benefit must be provided in regular intervals.
- Fixed – the amount of benefit must be fixed in nature or it may be fixed as a percentage of some component.
- Monetary – it must be given in monetary form.

When any or all of the above criteria are **not** fulfilled, the benefit cannot be considered as 'allowance'.

Types of Allowances and their Tax Treatment

The following is the list of various allowances usually given by employer to employee, their meaning and the tax treatment:

Sl. No.	Name of the Allowance	Meaning or Purpose of Allowance	Tax Treatment
1.	Dearness Allowance	An allowance given to enable employee to meet the rising cost of living. It is a very common allowance among all categories of employees and it is usually fixed as a percentage of 'Basic Salary'.	It is fully taxable Note: There is no condition to be fulfilled for charging dearness allowance

9.38 • Income Tax - I

Sl. No.	Name of the Allowance	Meaning or Purpose of Allowance	Tax Treatment
2.	City Compensatory Allowance	An allowance given to employees working in cities to enable them to meet the extra cost of living in cities. Similar to Dearness Allowance, this also is usually fixed as a percentage of 'Basic Salary'.	It is fully taxable .
3.	Travelling Allowance	It is an allowance granted to employee to enable him to meet the cost of travel on tour for <i>official purposes</i> or for meeting cost of transfer, including cost of packing and transportation of personal effects on such transfer.	It is exempt u/s 10(14) to the extent used for the said purpose.
4.	Conveyance Allowance	It is an allowance granted to meet the expenditure on conveyance in performance of duties of an office.	It is exempt u/s 10(14) to the extent used for the said purpose.
5.	Daily Allowance	It is an allowance 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.	It is exempt u/s 10(14) to the extent used for the said purpose.
6.	Helper Allowance	It is an allowance granted (by whatever name called) to meet the expenditure on employing a helper for providing assistance in the performance of duties of an office.	It is exempt u/s 10(14) to the extent used for the said purpose.
7.	Academic Allowance	It is an allowance (by whatever name called) granted for encouraging the academic, research and other professional pursuits of the employee.	It is exempt u/s 10(14) to the extent used for the said purpose.
8.	Uniform Allowance	It is an allowance (by whatever name called) granted to meet the expenditure on the purchase or maintenance of uniform for wear during the performance of duties of an office.	It is exempt u/s 10(14) to the extent used for the said purpose.
9.	Medical Allowance	It is an allowance granted to an employee for enabling him to meet the medical expenses of self and family.	It is fully taxable .
10.	Servant Allowance	It is an allowance granted to enable employees to engage services of domestic servants.	It is fully taxable .

Sl. No.	Name of the Allowance	Meaning or Purpose of Allowance	Tax Treatment
11.	Overtime Allowance	It is an allowance granted to employees who work overtime, for enabling them to meet the cost, if any, incurred during the period of overtime.	It is fully taxable .
12.	Breakfast Allowance or Lunch Allowance or Dinner Allowance or Refreshment Allowance	It is an allowance granted to enable employee in meeting his food expenses.	It is fully taxable .
13.	Project Allowance	It is an allowance granted when an employee is deputed on special projects.	It is fully taxable .
14.	Family Allowance	It is an allowance granted to an employee for enabling him to meet his household expenses.	It is fully taxable .
15.	Children Education Allowance	It is an allowance given to an employee for enabling him to meet the education expenses of his children.	It is exempt up to ₹100 per month per child for a maximum of two children under section 10(14).
16.	Hostel Expenditure Allowance	It is an allowance given to an employee for enabling him to meet the hostel expenses of his children.	It is exempt up to ₹300 per month per child for a maximum of two children under section 10(14).
17.	Transport Allowance	It is an allowance granted to employee for meeting travelling expenses for commuting between place of residence and place of his duty.	It is exempt under section 10 (14) up to ₹1,600 per month . (However, the exemption is up to ₹3,200 per month in case of employees who are blind, deaf, dumb or orthopedically handicapped).
18.	Transport Allowance to an employee working in a transport system	It is an allowance granted to an employee working in any transport system to meet his personal expenditure during the course of running of such transport from one place to another place provided that such employee is not in receipt of daily allowance.	It is exempt under section 10(14) to the extent of least of the following: 70% of the Allowance Or ₹10,000 per month.
19.	Allowances to Government Employees outside India	Any allowance given to Citizen of India, who is a Govt. employee, rendering services outside India.	It is fully exempt under section 10(7).

9.40 • Income Tax - I

Sl. No.	Name of the Allowance	Meaning or Purpose of Allowance	Tax Treatment
20.	Allowances to High Court Judges	They refer to allowances given in accordance with High Court Judges (Conditions of Service) Act, 1954.	It is fully exempt .
21.	Sumptuary Allowance given to High Court and Supreme Court Judges	Sumptuary Allowance refers to allowance given to Judges, which are in the nature of entertainment allowance.	It is fully exempt .
22.	Allowance received by an employee of United Nations Organisation		It is fully exempt .
23.	Non-practising Allowance	It is an allowance given to employees to compensate them for not practicing their profession separately – other than with employer.	It is fully taxable .
24.	Any other allowance for meeting personal expenses of the employee		It is fully taxable .
25.	Any other allowance for meeting expenses relating to performance of official duties		It is exempt to the extent used for the said purposes.
26.	Any other Special Allowances (Allowances against serial number 3, 4, 5, 6, 7, 8, 15, 16, 17 and 18 of this table are special allowances. Any other special allowances apart from them are covered here)		It is exempt to the extent specified under section 10(14) – see the next table.
27.	House Rent Allowance	It is an allowance given to employee to enable him to meet the rental expenses for his residential accommodation.	The tax provisions are explained separately.
28.	Entertainment Allowance	It is an allowance given to employee to enable him to meet expenses for entertaining guests and visitors to the business of employer.	It is fully taxable. However, Government Employees can claim deduction under section 16(ii) to the extent prescribed. [See details under ' Deductions under Section 16 '].

SPECIAL ALLOWANCES UNDER RULE 2BB & EXEMPT U/S 10(14)

(Other than the special allowances covered in the above list)

Name of Allowance	Maximum Amount Exempt from Tax
1. Any special compensatory allowance in the nature of special compensatory (hilly area) allowance or high altitude allowance or uncongenial climate allowance or snow bound area allowance or avalanche allowance. (a) Manipur, Arunachal Pradesh, Sikkim, Uttar Pradesh, Himachal Pradesh, specified areas of Jammu and Kashmir (b) Siachen area of Jammu and Kashmir (c) All other places located at a height of 1000 meters or more above the sea level other than places specified in A and B above.	₹ 800 p.m. ₹ 7,000 p.m. ₹ 300 p.m.
2. Any special compensatory allowance in the nature of Border Area Allowance, Remote Area Locality Allowance or Difficult Area Allowance or Disturbed Area Allowance. (a) Little Andaman, Nicobar and Narcondum Islands, North and Middle Andamans, throughout Lakshadweep and Minicoy Islands, specified areas of Himachal Pradesh, Chimpitupui District of Mizoram and areas beyond 25km from Lunglei town in Lunglei District of Mizoram, Specified area of Jammu and Kashmir, specified districts of Uttar Pradesh, Sikkim. (b) Installations in the continental shelf of India and the Exclusive Economic Zone of India. (c) Arunachal Pradesh, Nagaland, South Andaman (including Port Blair), Lunglei District of Mizoram, specified areas of Tripura, specified areas of Jammu and Kashmir, specified areas of Himachal Pradesh. (d) Aizawl district of Mizoram, Tripura, Manipur, specified areas of Himachal Pradesh, specified areas of Jammu and Kashmir. (e) Jog Falls in Shimoga District in Karnataka. (f) Other places of Himachal Pradesh, Assam and Meghalaya.	₹ 1,300 p.m. ₹ 1,100 p.m. ₹ 1,050 p.m. ₹ 750 p.m. ₹ 300 p.m. ₹ 200 p.m.
3. Special Compensatory (Tribal areas/scheduled areas/Agency areas) Allowance in Madhya Pradesh, Tamil Nadu, Uttar Pradesh, Karnataka, Tripura, Assam, West Bengal, Bihar, Orissa.	₹ 200 p.m.
4. Compensatory Field Area Allowance in specified areas of Arunachal Pradesh, Manipur, Nagaland, specified areas of Sikkim, specified areas of Himachal Pradesh, specified areas of Uttar Pradesh and specified areas of Jammu & Kashmir.	₹ 2,600 p.m.
5. Compensatory Modified Field Area Allowance in specified areas of Punjab and Rajasthan, specified areas of Haryana, specified areas of Himachal Pradesh, specified areas of Arunachal Pradesh and Assam, Mizoram, Tripura, specified areas of Sikkim and West Bengal, specified areas of Uttar Pradesh, specified areas of Jammu and Kashmir.	₹ 1,000 p.m.
6. Any special allowance in the nature of counter insurgency allowance granted to the members of the armed forces operating in areas away from their permanent locations.	₹ 3,900 p.m.

Name of Allowance	Maximum Amount Exempt from Tax
7. Underground allowance granted to an employee who is working in uncongenial, unnatural climate in underground coal mines.	₹ 800 p.m.
8. Any special allowance in the nature of high altitude (uncongenial climate) allowance granted to the member of the armed forces operating in high altitude areas (a) for altitude of 9,000 feet to 15,000 feet (b) for altitude above 15,000 feet	₹ 1,060 p.m. ₹ 1,600 p.m.
9. Any special allowance granted to the members of the armed forces in the nature of special compensatory highly active field area allowance.	₹ 4,200 p.m.
10. Any special allowance to the member of the forces in the nature of island allowance in Andaman, Nicobar and Lakshadweep.	₹ 3,250 p.m.

House Rent Allowance

‘House Rent Allowance’ refers to an allowance given to employee, to enable him to meet the rental expenses of his residential accommodation. This allowance is one among the standard set of allowances given to all categories of employees. Usually, it is fixed as a percentage of ‘Basic Salary’. So, where an employee is drawing a basic salary of ₹ 25,000 per month and is entitled for a House Rent Allowance @ 20%, then his House Rent Allowance is ₹ 5,000 per month.

The taxable amount of House Rent Allowance received by an employee is calculated using the following format, for **all** categories of employees:

	₹	₹
Actual House Rent Allowance		XXX
Less: Exempt under section 10(13A), being least of the following:		
(a) Actual amount of House Rent Allowance	XXX	
(b) Excess of ‘rent paid’ over 10% of “Salary”	XXX	
(c) 40% of “Salary”, being maximum limit	XXX	XXX
Taxable House Rent Allowance		XXX

Notes:

- “Salary” for this purpose includes:
 - Basic Salary
 - Dearness Pay
 - Dearness Allowance (if it enters into retirement benefits)
 - Commission based on a fixed percentage of turnover achieved by the employee.
- “Salary” must be calculated on ‘accrual’ basis. That is, the above items must be considered only for the period for which taxable HRA is being calculated, irrespective of whether they are received or not.

3. “Salary” must be calculated only for the period for which the Taxable HRA is calculated. Where, employee received HRA only for 8 months during the relevant previous year, “Salary” must be calculated only for those 8 months.
4. For item (b) in the above format, only rent amount **paid** must be considered. The proof for ‘payment of rent’ is the Rent receipt issued by the Landlord (owner) of the House. Unless otherwise stated, it can be assumed that rent has been paid.
5. Where the ‘rent paid’ is not exceeding 10% of “Salary”, the excess must be shown as ‘Nil’. For example, suppose that “Salary” for the purpose of HRA is ₹3,00,000 and rent paid is ₹2,000 per month. Then, ‘Rent paid’ is ₹24,000 for the year and 10% of “Salary” is ₹30,000. So, ‘rent paid’ is not exceeding 10% of “Salary”. Hence, item (b) in the above format will be shown as ‘Nil’ and not (–) ₹6,000.
6. Where the accommodation for which employee is paying rent is situated in Chennai, Delhi, Kolkata or Mumbai, 40% of “Salary” in the above format must be replaced by **50% of “Salary”**.
7. In the following three cases, the House Rent Allowance is fully taxable in the hands of the employee–
 - (a) Where the employee is residing in his own house or house owned by spouse, dependent children, dependent parents or the HUF in which the employee is a member;
 - (b) Where the employee is not incurring any expenditure for payment of rent; and
 - (c) Where the ‘rent paid’ by the assessee is not exceeding 10% of “Salary”.
 In all the above cases, the excess of ‘rent paid’ over 10% of “Salary” will be Nil and being the least, that will be exempted amount. When the amount exempted is ‘Nil’, the entire amount of House Rent Allowance is taxable.

Illustration 26 Problem on Computation of Taxable House Rent Allowance

Mrs. Anitha who resides in Chennai gets ₹60,000 p.a. as Basic Salary. She received ₹10,000 as House Rent Allowance. Rent paid by her was ₹8,000 p.a. Find out the taxable House Rent Allowance.

Solution:

Computation of Taxable House Rent Allowance

	₹	₹
Actual House Rent Allowance		10,000
Less: Exempt under section 10(13A), being least of the following:		
(a) Actual amount of House Rent Allowance	10,000	
(b) Excess of ‘rent paid’ over 10% of “Salary” [₹8,000 – ₹6,000]	2,000	
(c) 50% of “Salary”	30,000	2,000
Taxable House Rent Allowance		8,000

Notes:

1. Since the accommodation is in Chennai, 50% of “Salary” is considered for item (c) in the format.
2. “Salary” for HRA purpose.

	₹
1. Basic Salary	60,000
2. Dearness Allowance entering into retirement benefits	Nil
3. Fixed percentage of commission on turnover achieved by employee	Nil
	60,000

Illustration 27 Problem on Computation of Taxable House Rent Allowance

Ms. Bijli resides in Mysore and gets ₹40,000 p.a. as Basic Salary. She gets Dearness Allowance of 20% on her Basic Salary. Half of Dearness Allowance enters for retirement benefits. She receives ₹12,000 p.a. as House Rent Allowance though she pays ₹15,000 p.a. as house rent. Find out the taxable House Rent Allowance.

Solution:**Computation of Taxable House Rent Allowance**

	₹	₹
Actual House Rent Allowance		12,000
Less: Exempt under section 10(13A), being least of the following:		
(a) Actual amount of House Rent Allowance	12,000	
(b) Excess of ‘rent paid’ over 10% of “Salary” [₹15,000 – 4,400]	10,600	
(c) 40% of “Salary”	17,600	10,600
Taxable House Rent Allowance		1,400

Notes:

1. Since the accommodation is in Mysore, 40% of “Salary” is considered for item (c) above.
2. “Salary” for HRA purpose.

	₹
1. Basic Salary	40,000
2. Dearness Allowance entering into retirement benefits	4,000
3. Fixed percentage of commission on turnover achieved by employee	Nil
	44,000

Note: DA is 20% of salary i.e., ₹40,000 × 20% = ₹8,000. Half of it enters for retirement benefits. Hence, half of ₹8,000 i.e., ₹4,000 is considered for computing “Salary”.

Illustration 28 Problem on Computation of Taxable House Rent Allowance

Mr. Chakradhar resides in Delhi. He gets Basic Salary of ₹60,000 p.a. He is entitled for 20% Dearness Allowance. He receives ₹15,000 as House Rent Allowance but pays ₹18,000 as rent for the house in which he resides. Find out the taxable amount of House Rent Allowance.

Solution:

Computation of Taxable House Rent Allowance

	₹	₹
Actual House Rent Allowance		15,000
Less: Exempt under section 10(13A), being least of the following:		
(a) Actual amount of House Rent Allowance	15,000	
(b) Excess of ‘rent paid’ over 10% of “Salary” [₹18,000 – ₹6,000]	12,000	
(c) 50% of “Salary”	30,000	12,000
Taxable House Rent Allowance		3,000

Notes:

1. Since the accommodation is in Mysore, 40% of “Salary” is considered for item (c) above.
2. “Salary” for HRA purpose

	₹
1. Basic Salary	60,000
2. Dearness Allowance entering into retirement benefits	Nil
3. Fixed percentage of commission on turnover achieved by employee	Nil
	60,000

Note: DA is 20% of salary i.e., ₹60,000 × 20% = ₹12,000. However, it is not considered for computing “Salary” since it does not enter into retirement benefit,

Illustration 29 Problem on Computation of Taxable House Rent Allowance

Ms. Devi resides in Bangalore. She gets ₹80,000 p.a. as Basic Salary. She is entitled for 30% Dearness Allowance, half of which enters for retirement benefits. Besides other allowances she received ₹15,000 as House Rent Allowance but pays ₹12,000 as rent during the Previous Year 2017-18. She also receives advance salary of ₹8,000. Find out the exempted amount of House Rent Allowance for Assessment Year 2018-19.

Solution:

Exempted House Rent Allowance under section 10(13A) is least of the following:

	₹
(a) Actual amount of House Rent Allowance	15,000
(b) Excess of 'rent paid' over 10% of "Salary" [₹12,000 – ₹9,200]	2,800
(c) 40% of "Salary"	36,800

Exempted HRA is ₹2,800, being least of the above.

"Salary" for HRA purpose

	₹
1. Basic Salary	80,000
2. Dearness Allowance entering into retirement benefits	12,000
3. Fixed percentage of commission on turnover achieved by employee	Nil
	92,000

Notes:

- (a) DA is 30% of salary i.e., ₹80,000 × 30% = ₹24,000. Half of it enters for retirement benefits. Hence half of ₹24,000 i.e., ₹12,000 is considered for computing "Salary".
- (b) Advance salary should not be considered for calculation of "salary" for HRA purpose and hence ignored

Illustration 30 Problem on Computation of Taxable House Rent Allowance

Mr. Elango resides in Hassan. His emoluments for previous year 2017-18 are as under: Basic Salary ₹1,00,000; Dearness Allowance 25%; City Compensatory Allowance ₹12,000; Commission 2% on turnover (Actual turnover achieved by Mr. Elango during the Previous Year is ₹15,00,000); House Rent Allowance ₹40,000 (Rent paid ₹60,000); Arrears of salary ₹6,000; Leave Encashment ₹8,000. Find out taxable House Rent Allowance of Mr. Elango on the assumption that 60% of Dearness Allowance enters for retirement benefits.

Solution:**Computation of Taxable House Rent Allowance**

	₹	₹
Actual House Rent Allowance		40,000
Less: Exempt under section 10(13A), being least of the following:		
(a) Actual amount of House Rent Allowance	40,000	
(b) Excess of 'rent paid' over 10% of "Salary" [₹60,000 – ₹14,500]	45,500	
(c) 40% of "Salary"	58,000	40,000
Taxable House Rent Allowance		Nil

Notes:

1. Since the accommodation is in Hassan 40% of “Salary” is considered for item (c) above.
2. “Salary” for HRA purpose

	₹
1. Basic Salary	1,00,000
2. Dearness Allowance entering into retirement benefits	15,000
3. Fixed percentage of commission on turnover achieved by employee	30,000
	1,45,000

Notes:

- (a) DA is 25% of salary i.e., ₹1,00,000 × 25% = ₹25,000. 60% of it enters for retirement benefits. Hence, 60% of ₹25,000 i.e., ₹15,000 is considered for computing “Salary”.
- (b) Actual turnover achieved by Mr. Elango during the Previous Year is ₹15,00,000. Rate of commission is 2%. Hence 2% of ₹15,00,000 i.e., ₹30,000 is taken as commission on turnover achieved by employee.
- (c) City Compensatory Allowance, Arrears of salary and Leave Encashment are not part of “salary” for HRA purposes.

Illustration 31 Problem on Computation of Taxable House Rent Allowance

Ms. Fabida resides in Kolkata. She gets ₹12,000 p.a. as Basic Salary. She is entitled for Dearness Allowance at 20% which enters for retirement benefits. She has received commission of ₹15,000 (@ 2% on turnover). During the Previous Year 2017-18 she has received 30% of Basic Salary as House Rent Allowance but has paid ₹2,400 as rent to the landlord. Calculate the taxable House Rent Allowance.

Solution:**Computation of Taxable House Rent Allowance**

	₹	₹
Actual House Rent Allowance (₹12,000 × 30%)		3,600
Less: Exempt under section 10(13A), being least of the following:		
(a) Actual amount of House Rent Allowance	3,600	
(b) Excess of ‘rent paid’ over 10% of “Salary” [₹2,400 – ₹2,940]	Nil	
(c) 40% of “Salary”	14,700	Nil
Taxable House Rent Allowance		3,600

Notes:

1. Rent paid is less than 10% of salary and there is no “excess” of rent paid over 10% of salary. Hence, Nil is taken in item (b) above.
2. Since the accommodation is in Kolkata, 50% of “Salary” is considered for item (c) above.
3. “Salary” for HRA purpose

	₹
1. Basic Salary	12,000
2. Dearness Allowance entering into retirement benefits	2,400
3. Fixed percentage commission on turnover achieved by employee	15,000
	29,400

Illustration 32 Problem on Computation of Taxable House Rent Allowance

Calculate Taxable House Rent Allowance from the following information of Mr. Girish:

Basic Salary – ₹60,000 per month.

Dearness Allowance – 40% of Basic Salary (75% of Dearness Allowance enters into retirement benefits)

Commission on Sales achieved by Girish – 2%. (During previous year 2016-17, Girish achieved a turnover of ₹5,00,000).

House Rent Allowance – 20% of Basic Salary.

Other Allowances – ₹10,000 per month.

Rent paid by Girish for his residence in Bangalore – ₹11,000 per month.

Solution:**Computation of Taxable House Rent Allowance**

	₹	₹
Actual House Rent Allowance (₹12,000 × 12)		1,44,000
Less: <i>Exempt under section 10(13A), being least of the following:</i>		
(a) Actual amount of House Rent Allowance	1,44,000	
(b) <i>Excess</i> of ‘rent paid’ over 10% of “Salary” [₹1,32,000 – (₹9,46,000 × 10/100)]	37,400	
(c) 40% of “Salary” (₹9,46,000 × 40/100)	3,78,400	37,400
Taxable House Rent Allowance		1,06,600

Notes:

1. House Rent Allowance is 20% of Basic Salary. Hence, HRA per month is ₹12,000 (i.e., ₹60,000 × 20/100).

2. In the absence of information, it is assumed that all factors remain same for the entire previous year.
3. Since the accommodation is in Bangalore, 40% of “Salary” is considered for item (c) in the format.
4. ‘Rent paid’ for previous year 2017-18 is ₹1,32,000 (i.e., ₹11,000 × 12).
5. “Salary” for the purpose of House Rent Allowance

	₹
Basic Salary (₹60,000 × 12)	7,20,000
Dearness Allowance (₹7,20,000 × 40/100 × 75/100)	2,16,000
Commission on Sales achieved by employee (₹5,00,000 × 2/100)	10,000
	9,46,000

Note: Dearness Allowance is considered only to the extent it enters into retirement benefits.

Illustration 33 Problem on Computation of Taxable House Rent Allowance, when there are changes in various factors

Mr. Mohit is employed with XY Ltd. on a basic salary of ₹10,000 per month. 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 ₹6,000 per month which was increased to ₹7,000 per month with effect from 01-01-2018. He also got an increment of ₹1,000 per month in his basic salary with effect from 01-02-2018. Rent paid by him during the previous year 2017-18 is as under:

April and May 2017 – Nil, he stayed with his parents.

June to October 2017 – ₹6,000 per month for an accommodation in Ghaziabad.

November 2017 to March 2018 – ₹8,000 per month for an accommodation in Delhi.

Compute his gross salary for assessment year 2018-19.

Solution:

Computation of Gross Salary of Mr. Mohit

	₹	₹
Basic Salary [(₹10,000 × 10) + (₹11,000 × 2)]		1,22,000
Dearness Allowance [100% of Basic Salary]		1,22,000
Taxable House Rent Allowance (See Working Note below)		21,300
Gross Salary		2,65,300

Working Note: Computation of Taxable House Rent Allowance

(₹)

Particulars	Apr 2017	May 2017	Jun 2017	July 2017	Aug 2017	Sep 2017	Oct 2017	Nov 2017	Dec 2017	Jan 2018	Feb 2018	Mar 2018
1. Actual HRA	6000	6000	6000	6000	6000	6000	6000	6000	6000	7000	7000	7000
2. Rent Paid	Nil	Nil	6000	6000	6000	6000	6000	8000	8000	8000	8000	8000
3. "Salary" Bas. Salary	10000	10000	10000	10000	10000	10000	10000	10000	10000	10000	11000	11000
D Allowance	5000	5000	5000	5000	5000	5000	5000	5000	5000	5000	5500	5500
	15000	15000	15000	15000	15000	15000	15000	15000	15000	15000	16500	16500
4. 10% of Salary	1500	1500	1500	1500	1500	1500	1500	1500	1500	1500	1650	1650
5. Excess of Rent paid over 10% of Sal- ary (2 minus 4)	Nil	Nil	4500	4500	4500	4500	4500	6500	6500	6500	6350	6350
6. Place of Accommodation	Ghaziabad						Delhi					
7. Max. Limit (% of "Salary")	40%	40%	40%	40%	40%	40%	40%	50%	50%	50%	50%	50%
8. Max. Limit	6000	6000	6000	6000	6000	6000	6000	7500	7500	7500	8250	8250
9. HRA Exempt (least of 1, 5 and 8)	Nil	Nil	4500	4500	4500	4500	4500	6000	6000	6500	6350	6350
10. Taxable HRA (1 minus 9)	6000	6000	1500	1500	1500	1500	1500	Nil	Nil	500	650	650

Total Taxable HRA for previous year 2017-18 = ₹21,300.

Notes:

1. Since, the factors influencing taxable HRA are not constant for the entire previous year, it was necessary to calculate exempted and taxable HRA for each month separately.
2. Dearness Allowance is 100% of Basic Salary. However, only 50% of DA enters into retirement benefits and hence, only that is included in computing “Salary” for the purpose of HRA.

DEDUCTIONS UNDER SECTION 16

9.8

The following deductions can be claimed from ‘Gross Salary’ under section 16, in the process of computing ‘taxable salary’:

1. Entertainment Allowance [Section 16(ii)]
2. Employment or Professional Tax [Section 16(iii)]

9.8.1 Entertainment Allowance under Section 16(ii)

Entertainment Allowance is an allowance given to employee for enabling him to meet expenses for entertaining visitors and customers of the employer. Entertainment Allowance received by an employee is taxable under ‘Allowances’. However, where the employee is a **Government Employee**, he can claim deduction for entertainment allowance under section 16(ii). The amount of deduction is **least** of the following:

- (a) 20% of ‘Basic Salary’ of the relevant previous year.
- (b) Maximum limit of ₹5,000.
- (c) Actual amount of Entertainment Allowance for the relevant previous year.

Note: The deduction for entertainment allowance is available only to government employees. The actual amount spent by the employee towards entertaining customers and visitors, is not considered in calculating the amount of deduction.

9.8.2 Professional Tax or Employment Tax under Section 16(iii)

Professional Tax is a tax levied by State Governments on employees and professionals, in accordance with the Constitution of India. Each State has its own policy regarding professional tax and the amount of professional tax levied varies from one State to another.

Any professional tax **paid** during previous year, in the name of employee is deductible under section 16(iii).

Notes:

1. Professional tax is deductible from ‘Gross Salary’ only when it is **paid**.
2. The payment of professional tax of employee may be made by employee himself or employer.

3. The amount of professional tax *paid* during the relevant previous year is completely deductible, irrespective of the period to which the professional tax belongs to.

9.9

PROVIDENT FUND

Provident Fund is a fund which provides for the future of employees. It is a type of savings scheme for the future benefit of employees. When an individual gets employed, he automatically becomes member of the Provident Fund Scheme maintained by his employer. Every month the employee makes a contribution to his Provident Fund Account (by way of deduction from salary and credit to provident fund account), and usually, a matching contribution is made by employer to the provident fund account of the employee.

The contribution of both employer and employee is invested, on which interest accrues. The interest on such investment is credited to the provident fund account, and along with the contribution of the next period, it is further invested. This process of contribution, investment, interest accrual, further contribution, investment etc., happen till the retirement, resignation or death of employee. At the time of retirement, or resignation or death of employee, the accumulated balance in the provident fund account will be withdrawn by the employee, or his legal heirs.

Types of Provident Fund

The following are the different types of Provident Fund:

1. Statutory Provident Fund
2. Recognised Provident Fund
3. Unrecognised Provident Fund
4. Approved Superannuation Fund
5. Public Provident Fund

A brief explanation of each type of provident fund, is provided below:

Statutory Provident Fund is a fund which is set up, maintained and managed in accordance with the provisions of a Statute – the Provident Fund Act, 1925. This type of provident fund is usually found in Government organisations, semi-government organisations, universities, educational institutions affiliated to recognised universities, etc.

Recognised Provident Fund is a fund which is recognised under the Provident Funds and Miscellaneous Provisions Act, 1952. It is a fund which is either set up by the Provident Fund Commissioner under the Provident Fund Act, 1952 or a fund set up and managed by the employer, for which approval has been granted by the Provident Fund Commissioner. This is the type of provident fund, which is widely found in organisations.

Unrecognised Provident Fund is a fund which is neither statutory, nor recognised. It is a fund set up and managed by the employer, for which approval has not yet been granted by the Provident Fund Commissioner.

Approved Superannuation Fund is a type of fund, in which, annuities or regular payments become payable to the members (i.e., employees) only on employees attaining a specified age or after retirement of employee or on incapacitation or death of the employee. It is run, operated and managed by employer through separate trusts. When the superannuation fund run by an employer is granted approval by the Income Tax Commissioner, it becomes ‘approved superannuation fund’.

Public Provident Fund is a provident fund scheme operated by the Central Government, for the benefit of general public. Public Provident Fund scheme is not between employer and employee, but between the Government and the general public. In this type of provident fund, only the member makes a contribution to the provident fund account, but no contribution is made by the Government.

Tax Treatment Relating to Provident Fund

From the operation of provident fund given earlier, the following items call for attention from tax perspective:

1. Employee’s contribution to his provident fund account.

This is not an income, but a saving made by the assessee. Any tax benefit available to this must be provided to the assessee. The availability of tax benefit for this depends on the type of provident fund of which the employee is member of.

2. Employer’s contribution to employee’s provident fund account

This is a ‘deemed receipt’ in the hands of an employee and hence taxable. Being benefit from employer, it must be charged under the head “Income from Salaries”. The tax treatment for this depends on the type of provident fund of which the employee is member of.

3. Interest on accumulated balance of provident fund

This is an income earned by the assessee. Where the provident fund membership of the assessee is on account of his employment, interest on accumulated balance of provident fund must be charged under the head “Income from Salaries”. Where the provident fund membership of the assessee is not on account of his employment (like public provident fund), then the interest income must be shown under the head “Income from Other Sources”. The tax treatment for interest income on provident fund depends on the type of provident fund of which the employee is member of.

4. Accumulated Balance Withdrawn

This is a capital receipt and usually, is not taxable. However, it is taxable in certain circumstances and the tax treatment for the same depends on the type of provident fund of which the employee is member of.

Under the head “Income from Salaries” two items relating to provident fund must be considered for tax purposes, viz., employer’s contribution to provident fund account of the employee and interest on accumulated balance of provident fund. It would be most preferable to show these items after “allowances”, and before computing taxable value of perquisites.

9.54 • Income Tax - I

The tax treatment for all the above four items under each type of provident fund is summarised in the following table:

	Statutory Provident Fund	Recognised Provident Fund	Unrecognised Provident Fund	Approved Superannuation Fund	Public Provident Fund
Assessee's Contribution to his provident fund account	Deductible u/s 80C	Deductible u/s 80C	No tax benefit	Deductible u/s 80C	Deductible u/s 80C
Employer's Contribution to employee's provident fund account	Exempt	Taxable to the extent the contribution exceeds 12% of 'Salary'	Ignored	Taxable under 'Perquisites' to the extent contribution exceeds ₹ 1,50,000	—
Interest on Accumulated Balance	Exempt	Taxable to the extent, the interest exceeds 9.5%	Ignored	Exempt	Exempt
Accumulated Balance Withdrawn	Exempt	Exempt if at least 5 years of service has been rendered	Employer's contribution + Interest thereon – taxable under "Salaries". Interest on employee's contribution – taxable under 'Income from Other Sources'	Exempt	Exempt

Notes:

1. For assessee's contribution to his provident fund account, tax benefit is available in the form of deduction u/s 80C from Gross Total Income, in case of Statutory, Recognised, Approved and Public Provident Funds.
2. Employer's contribution to the recognised provident fund account of the employee is exempt up to 12% of "salary" for this purpose; and any excess contribution over and above 12% of "Salary" is taxable.
3. "Salary" for this purpose includes basic salary, dearness pay, dearness allowance (if it enters into retirement benefits) and commission based on a fixed percentage of turnover achieved by employee. The "salary" must be calculated on "accrual" basis.

4. The interest accrued on accumulated balance of recognised provident fund is **exempt up to 9.5%** and only the excess interest over and above 9.5% rate of interest is taxable. For example, suppose Interest of ₹24,000 is credited to the recognised provident fund account of the employee during relevant previous year, @ 12%. Then the excess interest equivalent to 2.5% is taxable. That is, ₹5,000 ($₹24,000 \times 2.5/12$) will be the taxable value.
5. Accumulated balance withdrawn from recognised provident fund account is exempt in the hands of the employee, when the employee has rendered at least 5 years of continuous service. Otherwise, the treatment applicable for accumulated balance withdrawn from 'unrecognised provident fund' will be applicable in this case also.
6. In case of unrecognised provident fund, tax treatment is ignored every year for employer's contribution and interest. However, the same will be taxable when accumulated balance is withdrawn from the provident fund account.
7. There is no contribution by the Government or any other person in case of Public Provident Fund.

Transferred Balance

When an un-recognised provident fund gets recognised, the balance standing in the provident fund account at the time of recognition is called 'transferred balance'. In the year of recognition, there is a tax implication in the hands of the employee that needs to be considered. Till the date of recognition, employer's contribution to employee's provident fund account and interest credited to the account would have been ignored from being charged to tax. So, at the time of recognition, the 'transferred balance' must be taxable to the extent the employer's contribution and interest thereon.

Illustration 34 Problem on tax treatment for provident fund

For the previous year 2017-18, X provides the following information:

Basic salary – ₹1,80,000; dearness allowance – ₹60,000, (46 per cent of which is **part of salary for retirement benefits**); commission: ₹9,000 (i.e., 1.5 per cent of ₹6,00,000, being turnover achieved by X) and children education allowance for his 2 children: ₹7,200. The employer contributes ₹30,000 towards provident fund to which a matching contribution is made by X. Interest credited in the provident fund account on March 15, 2018 @ 14 per cent comes to ₹1,19,000.

Find out the taxable salary of X for the assessment year 2018-19 if the provident fund is

- (a) statutory provident fund,
- (b) recognized provident fund,
- (c) unrecognized provident fund.

Solution:

**Computation of Taxable Salary of Mr. X for Assessment Year 2018-19
(Previous Year 2017-18)**

	When X is a member of–		
	Statutory Provident Fund ₹	Recognised Provident Fund ₹	Un-recognised Provident Fund ₹
Basic Salary	1,80,000	1,80,000	1,80,000
Commission	9,000	9,000	9,000
Dearness Allowance	60,000	60,000	60,000
Children Education Allowance 7,200			
Less: Exempt under section 10(14)- (₹100 × 12 × 2) 2,400	4,800	4,800	4,800
Employer's Contribution to Provident Fund (See Working Note)	Exempt	4,008	Ignored
Interest on accumulated balance of provident fund (See Working Note)	Exempt	38,250	Ignored
Gross Salary	2,53,800	2,96,058	2,53,800
Less: Deductions under section 16	Nil	Nil	Nil
Taxable Salary	2,53,800	2,96,058	2,53,800

Working Notes:

- Employer's contribution towards Statutory Provident Fund of the employee and interest credited to the account are exempt from tax.
- Employer's Contribution towards Un-recognised Provident Fund and interest credited to the account are ignored for the time-being, and are taxable at the time of withdrawal of accumulated balance from the account.
- Employer's contribution towards Recognised Provident Fund is taxable to the extent the contribution exceeds 12% of "Salary". The excess contribution is calculated as follows:
 - "Salary" for the purpose of Recognised Provident Fund

	₹
Basic Salary	1,80,000
Dearness Allowance (46% of ₹60,000)	27,600
Commission based on a fixed percentage of turnover achieved by X	9,000
	2,16,600

- Computation of taxable extent of employer's contribution to Provident Fund

	₹
Employer's Contribution	30,000
Less: 12% of "Salary" (12% of ₹2,16,600)	25,992
	4,008

Interest credited to recognised provident fund account of the employee is taxable to the extent the interest exceeds 9.5%. In this case, the interest credited to the account during previous year is ₹1,19,000 @ 14%. Therefore, the interest is in excess by 4.5% over and above the prescribed rate. Hence, the proportionate amount of interest [i.e., ₹1,19,000 × 4.5/ 14 = ₹38,250] is taxable.

Illustration 35 Problem on Calculation of Taxable Salary involving allowances, contribution to provident fund and deductions

Mr. M is an area manager of M/s N Steels Co. Ltd. During the financial year 2017-18, he gets the following emoluments from his employer:

	₹
Basic Salary	
• Up to 31.08.2017	20,000 per month
• From 01.09.2017	25,000 per month
Dearness Allowance	20%
Transport allowance	2,800 per month
Contribution to recognized provident fund	15% of 'Basic Salary and DA'
Children education allowance	500 p.m. for two children
City compensatory allowance	300 per month.
Hostel expenses allowance	380 p.m. for two children
Tiffin allowance (actual expenses ₹3,700)	5,000 per annum
Tax paid on employment	2,500

Compute the taxable salary of Mr. M for the assessment year 2018-19.

Solution:

Computation of Taxable Salary of Mr. M for Assessment Year 2018-19 (Previous Year 2017-18)

	₹	₹
Basic Salary [(₹20,000 × 5) + (₹25,000 × 7)]		2,75,000
Dearness Allowance (20% of ₹2,75,000)		55,000
City Compensatory Allowance (₹300 × 12)		3,600
Transport Allowance (₹2,800 × 12)	33,600	
Less: Exempt u/s 10(14) – (₹1,600 × 12)	<u>19,200</u>	14,400

	₹	₹
Children Education Allowance ($₹500 \times 12 \times 2$)	12,000	
Less: Exempt u/s 10(14) – ($₹100 \times 12 \times 2$)	<u>2,400</u>	9,600
Hostel Expenditure Allowance ($₹380 \times 12 \times 2$)	9,120	
Less: Exempt u/s 10(14) – ($₹300 \times 12 \times 2$)	<u>7,200</u>	1,920
Tiffin Allowance (fully taxable)		5,000
Employer's Contribution to Recognised Provident Fund (See Working Note)		9,900
Gross Salary		<u>3,74,420</u>
Less: Deductions under section 16		
(ii) Entertainment Allowance (Not available)	–	
(iii) Employment tax paid	<u>2,500</u>	2,500
Taxable Salary		3,71,920

Working Note:

Calculation of taxable amount of employer's contribution to employee's recognised provident fund account:

1. "Salary" for this purpose:

	₹
Basic Salary	2,75,000
Dearness Allowance (fully enters into retirement benefits)	<u>55,000</u>
	3,30,000

Note: Contribution to recognised provident fund is 15% of 'Basic Salary and DA'. It means for calculating the contribution, entire DA must be considered. Hence, entire amount of DA enters into retirement benefits.

2. Taxable amount of contribution

	₹
Employer's Contribution (15% of ₹3,30,000)	49,500
Less: 12% of "Salary" (12% of ₹3,30,000)	<u>39,600</u>
	9,900

PERQUISITES UNDER SECTION 17(2)**9.10**

A perquisite is a casual emolument, fee or profit, attached to an office or position in addition to the salary or wages. It refers to benefits provided to employee which results in personal advantage to the employee, and **does not fulfill** at least one of the following criteria:

- (a) Regular
- (b) Fixed
- (c) Monetary

(**Note:** When all the above criteria are fulfilled, the benefit will be considered as an allowance).

The following examples help in differentiating between allowances and perquisites:

1. X is given ₹500 per month by his employer towards medical expenses. This is an allowance. Where the medical expenses are reimbursed by employer, it is a perquisite.
2. Employee is given ₹1000 per month for meeting travel expenses between residence and place of work. This is 'transport allowance'. Employer provides transport facility for picking and dropping of employee from residence to place of work, and vice versa. This is a case of perquisite.
3. Employee is given ₹2500 per month for meeting lunch expenses. This is 'lunch allowance'. Where the employer himself provides food facility in the company premises, or through tokens that can be exchanged at food joints, it is a case of perquisite.

Chargeability of Perquisites

Perquisites are taxable under the head "Income from Salaries" when—

- (a) they are given by employer to employee;
- (b) during service period;
- (c) for services rendered by employee to employer organisation.

Classification of Perquisites

Based on tax-treatment, perquisites are classified into the following categories:

- A. Tax-free Perquisites.
- B. Taxable Perquisites—
 - (a) Taxable in the hands of all employees;
 - (b) Taxable in the hands of 'specified employees' only.

9.10.1 Tax Free Perquisites

They refer to perquisites which need not be 'recognised' for tax purposes. The following is the list of various tax-free perquisites:

1. ***In respect of Rent-free Accommodation:***
 - (a) Rent-free official residence provided to Judges of High Court and Supreme Court.
 - (b) Rent-free residence provided to an Official of Parliament, a Union Minister and a Leader of the Opposition.
 - (c) Accommodation located in 'remote area' (i.e., an area located at least 40 kilometers away from a town having a population not exceeding 20000), provided to an employee working at a mining site or an onshore oil exploration site, or a project execution site or a dam site or power generation site or an offshore site.

- (d) Accommodation of temporary nature (and having a plinth area of 800 sq. ft or less) which is located at least 8 km away from the local limits of a municipality or a cantonment board provided to an employee working at a mining site or an onshore oil exploration site, or a project execution site or a dam site or power generation site or an offshore site, is not chargeable to tax.
 - (e) When an employee is in possession of more than one accommodation on account of transfer from one place to another, value of one accommodation is not chargeable for first 90 days.
 - (f) Hotel accommodation provided to employee on his transfer from one place to another place, for a period not exceeding 15 days is not chargeable to tax.
- 2. In respect of interest-free or concessional interest loan given by employer to employee:**
- (a) Loan made available for medical treatment in respect of diseases specified in rule 3A.
 - (b) Where the aggregate amount of original loan does not exceed ₹20,000.
- 3. In respect of lunch/refreshment etc:**
- (a) Food and non-alcoholic beverages provided in working hours in remote area or in an offshore installation.
 - (b) Tea or snacks provided during working hours.
 - (c) Food and non-alcoholic beverages provided in office premises or through non-transferable paid vouchers usable only at eating joints provided by an employer up to ₹50 per meal.
- 4. Gifts in kind up to ₹5,000 in aggregate per annum would be exempt.**
- 5. In respect of credit card facility:**
- Expenditure on use of credit card for official purposes is not chargeable to tax, provided—
- (a) Complete details in respect of such expenditure is maintained by the employer which may *inter alia*, include the date of expenditure and the nature of expenditure,
 - (b) 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.
- 6. In respect of club facility:**
- (a) Health club, sports facilities, etc., provided uniformly to all classes of employees by the employer at employer's premises are exempt. Consequently, expenditure on such facility is not included.
 - (b) The initial one time deposit or fees for corporate or institutional membership, where benefit does not remain with a particular employee after cessation of employment are exempt.
 - (c) Expenditure on use of club facility for official purposes is exempt from tax provided—

- (i) Complete details in respect of such expenditure is maintained by the employer which may, inter-alia, include the date of expenditure, the nature of expenditure and its business expediency.
- (ii) 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.

7. *Computers or lap tops, and telephone provided by employer to employee are exempt from tax.*

8. *In respect of motor car facility:*

- (a) Car provided by employer to employee and used by employee completely for official purposes is not chargeable to tax provided—
 - (i) The employer has maintained complete details of journey undertaken for official purposes which may include date of journey, destination, mileage, and the amount of expenditure incurred thereon.
 - (ii) The employer gives a certificate to the effect that the expenditure was incurred wholly and exclusively for the performance of official duties.
- (b) Conveyance facility provided to Judges of High Court and Supreme Court is not chargeable to tax.
- (c) The use of motor car by an employee for the purpose of going from his residence to the place where the duties of employment are to be performed or from such place back to his residence, is not chargeable to tax.
- (d) Car owned by employee, expenses for which are met by employer, if used completely for official purposes is not chargeable to tax provided—
 - (i) The employer has maintained complete details of journey undertaken for official purposes which may include date of journey, destination, mileage, and the amount of expenditure incurred thereon.
 - (ii) The employer gives a certificate to the effect that the expenditure was incurred wholly and exclusively for the performance of official duties.
- (e) When car owned by employee is used by him for both official and personal purposes, expenses for which are met by employer, the facility is exempt up to ₹1800 p.m. (if the cc rating of the car does not exceed 1600) or ₹2400 p.m. (if the cc rating of the car exceeds 1600) provided—
 - (i) The employer has maintained complete details of journey undertaken for official purposes which may include date of journey, destination, mileage, and the amount of expenditure incurred thereon.
 - (ii) The employer gives a certificate to the effect that the expenditure was incurred wholly and exclusively for the performance of official duties.

9. *In respect of any other conveyance facility:*

Vehicle owned by employee, expenses for which are met by employer, if used completely for official purposes is not chargeable to tax provided—

- (iii) The employer has maintained complete details of journey undertaken for official purposes which may include date of journey, destination, mileage, and the amount of expenditure incurred thereon.
- (iv) The employer gives a certificate to the effect that the expenditure was incurred wholly and exclusively for the performance of official duties.

10. *In respect of free or concessional education:*

- (a) Amount spent for providing free education facilities to, and training of, the employees is not taxable.
- (b) When employee's children is provided free or concessional education in an institution owned and maintained by employer, the cost of education or value of such benefit is exempt **up to ₹1000 per month per child**.
- (c) Amount of scholarship given by employer-company to children of its employees solely at its discretion without reference to terms of employment is not assessable as perquisite in the hands of employees.

11. *Free transportation facility provided to employees and 'members of their household' by Railways and Airlines.*

12. *Premium paid by employer on personal accident policy in the name of employee, policy being taken by employer.*

13. *Employer's contribution to Group Insurance Scheme of Employees.*

14. *Sale of goods manufactured by employer at concessional rates.*

**15. *Tax paid by employer on non-monetary perquisites provided to employee* [Section 10(10CC)].
– (explained under the head "Profits and Gains from Business or Profession")**

16. *Medical Facilities:*

- (a) Expenses incurred by employer on medical treatment of employee or his family members in a hospital maintained by employer.
- (b) Expenses incurred or reimbursed by employer on medical treatment of employee or his family members in a hospital maintained by Central Government or State Government or Local Authority.
- (c) Expenses incurred or reimbursed by employer on medical treatment of employee or his family in a hospital approved by the Chief Commissioner for treatment of disease prescribed under Rule 3A.
- (d) In any other case – up to ₹15000 per annum is exempt.
- (e) Medical Insurance Premium paid or reimbursed by employer on policy of employee and his family.
- (f) Medical Treatment outside India
 - (i) Medical treatment expenses met by employer – exempt to the extent permitted by Reserve Bank of India.
 - (ii) Lodging and Boarding expenses of patient and one attendant met by employer – exempt to the extent permitted by Reserve Bank of India.

- (iii) Travelling expenses of patient and one attendant met by employer – fully exempt if the gross total income of the employee (before considering this benefit) does not exceed ₹2,00,000.

Note: For the purpose of this benefit, “family” means–

- The spouse and children of the individual; and
- The parents, brothers and sisters of the individual or any of them, wholly and mainly dependent on the individual.

17. In respect of leave travel concession:

Leave travel concession extended by an employer to an employee for going anywhere in India along with his family is exempt twice in a block of four years to the extent of *least* of the following:

- (a) Amount of assistance provided by employer; or
- (b) Actual expenditure on travel incurred by employee; or
- (c) Amount as per guidelines under rule 2B.

The amount as per guidelines is as follows:

Situation	Amount as per guidelines
When the journey is performed by air	Amount of economy class air fare of the national carrier by the shortest route to the destination.
Where journey is performed by rail	Amount of air-conditioned first class rail fare by the shortest route to the destination.
Where the journey is by some other mode and the place of origin and place of destination is connected by rail	Amount of air-conditioned first class rail fare by the shortest route to the destination.
Where the journey is by some other mode and the place of origin and place of destination is not connected by rail. However, a recognized public transport system exists between the two places.	First class or deluxe class fare by the shortest route to the destination.
Where the journey is by some other mode and the place of origin and place of destination is not connected by rail; and no recognized public transport system exists between the two places.	Air-conditioned first class rail fare for distance equivalent to the shortest route to the destination (as if the journey had been performed by rail)

Note: For the purpose of this benefit, “family” means–

- (a) The spouse and children of the individual; and
- (b) The parents, brothers and sisters of the individual or any of them, wholly and mainly dependent on the individual.

‘Children’ of the individual include–

- (i) All surviving children of the employee, born before 1st October 1998.

- (ii) Up to two surviving children born on or after 1st October 1998.
- (iii) After 1st October 1998, where a child is born and in the next birth, if multiple children are born, then children born out of multiple births after the first child will be treated as one child.

Illustration 36 Problem on tax-treatment for medical benefits

State whether the following is exempt or taxable in the hands of X, an employee of ABC Ltd.

1. Free medical treatment to X in the hospital run by ABC Ltd..
2. Expenditure incurred by ABC Ltd., on medical treatment of Mrs. X and her mother in a Government Hospital – ₹1,00,000 each.
3. Expenditure on medical treatment of X's father (wholly dependent on X) in an approved public hospital, reimbursed by ABC Ltd. – ₹50,000.
4. Medical Insurance Premium of X, Mrs. X, their son aged 25 (not dependent on X), and brother of X (wholly dependent on X) paid by ABC Ltd. – ₹5000 on policy of each person.
5. Expenditure on medical treatment of X's sister in a private hospital, met by ABC Ltd. – ₹25,000. (X's sister is mainly dependent on X.)
6. Expenditure on medical treatment of X's second brother in a private hospital, completely reimbursed by ABC Ltd. – ₹1,00,000. His second brother is not dependent on X.

Solution:

The tax treatment in each case is shown in the table below:

Case Number	Transaction	Tax Treatment
Case 1	Free medical treatment to X in the hospital run by ABC Ltd.	The benefit is completely exempt in the hands of X.
Case 2	Expenditure incurred by ABC Ltd. on medical treatment of Mrs. X and her mother in a Government Hospital – ₹1,00,000 each.	Expenditure incurred by employer on medical treatment of Mrs. X is exempt. However, expenditure incurred on Mrs. X's mother is fully taxable in the hands of X, since 'mother-in-law' is not a part of 'family' for this purpose.
Case 3	Expenditure on medical treatment of X's father (wholly dependent on X) in an approved public hospital, reimbursed by ABC Ltd. – ₹50,000.	This benefit is completely exempt in the hands of X.
Case 4	Medical Insurance Premium of X, Mrs. X, their son aged 25 (not dependent on X), and brother of X (wholly dependent on X) paid by ABC Ltd. – ₹5000 on policy of each person.	The entire amount of medical insurance premium paid by employer is exempt. Note: Children, whether dependent or not, are considered as part of 'family'.

Case Number	Transaction	Tax Treatment
Case 5	Expenditure on medical treatment of X's sister in a private hospital, met by ABC Ltd. – ₹25,000. (X's sister is mainly dependent on X).	This benefit given by employer is exempt up to ₹15,000 and the balance of ₹10,000 is taxable in the hands of X.
Case 6	Expenditure on medical treatment of X's second brother in a private hospital, completely reimbursed by ABC Ltd. – ₹1,00,000. His second brother is not dependent on X.	Since the brother is not dependent on X, he is not a part of 'family'. Hence, any expenditure on medical treatment of his second brother, met or reimbursed by employer, is fully taxable in the hands of X.

Illustration 37 Problem on tax-treatment of Leave Travel Concession

Rajesh went to Shrinagar on a holiday on 15-11-2017 with his wife and two children (one son aged – 6 years; twin daughters – aged 3 years). They went by aero-plane (economy class) and the total cost of tickets met by his employer was ₹58,000 (₹43,000 for adults and ₹15,000 for the three minor children).

Compute the amount of Leave Travel Concession exempt.

Will the answer be any different if among his three children the twins are 6 years old and son 3 years old? Discuss.

Solution:

The exemption for Leave Travel Concession u/s 10(5) is *least* of the following:

- Actual travel expenses incurred for employee and 'family members'.
- Amount as per guidelines.
- Amount of leave travel concession received.

In this case,

- Actual travel expenses incurred are ₹58,000. (since twins are born after first child, they are considered as two children. Hence, travel expenses of all three children have been considered).
- Amount as per guideline – since the travel is by economy class, the actual expenditure of ₹58,000 itself is considered as the amount as per guideline.
- Amount of benefit received from employer towards travel – ₹58,000.

Since, all the three limits are same, the amount of exemption is **₹58,000**

Where, the twins were born first and then the single child, only the twins will be considered – since only two surviving children born after 1.10.1998 are included in 'family'.

Accordingly,

- Actual travel expenses of employee and family is ₹53,000 (excluding the travel cost of son).

(ii) Amount as per guideline – ₹53,000.

(iii) Amount of benefit received from employer – ₹58,000.

Least of the above is ₹53,000 and hence is exempt from tax u/s 10(5).

9.10.2 Perquisites Taxable in the Hands of All Employees

The following perquisites are taxable in the hands of all employees, **irrespective of their category, position, pay or any other criteria:**

1. Rent-free accommodation [Section 17(2)(i)]
2. Accommodation provided at concessional rent [Section 17(2)(ii)]
3. Personal obligation of employee paid/reimbursed by employer [Section 17(2)(iv)]
4. Insurance premium paid by employer on life insurance policy of employee, policy being taken by employer [Section 17(2)(v)]
5. Free on concessional allotment of shares under Employee Stock Option Plan or Sweat Equity Shares. [Section 17(2)(vi)]
6. Contribution by employer to employee's approved superannuation fund [Section 17(2)(vii)]
7. Any other fringe benefits [Section 17(2)(viii)].

The tax treatment and valuation of each of the above perquisites are explained below:

Rent Free Accommodation [Section 17(2)(i)]

Where the employer has provided accommodation to the employee and his family, without charging any rent, it is a perquisite taxable under section 17(2)(i). The taxable value of rent-free accommodation must be ascertained in accordance with the provisions specified under Income Tax Rule 3(1).

The various cases when rent-free accommodation is **not taxable** are given under '**tax-free perquisites (Item No. 1)**'. In other cases, the benefit is taxable and following are the valuation provisions pertaining to rent-free accommodation:

The accommodation provided by employer to employee may be–

1. House Accommodation, or
2. Hotel Accommodation

Valuation of Rent-free House Accommodation provided to employee

The valuation of rent-free house accommodation provided to employee depends upon whether the accommodation provided is 'Unfurnished' or 'Furnished'.

Valuation of Rent-free Unfurnished House Accommodation

The provisions for valuation of rent-free unfurnished house accommodation is summarised in the following table:

Value of Rent Free Unfurnished House Accommodation provided to Employees under Government Service	License Fee determined by the Central Government or State Government in accordance with the rules framed by the Government for allotment of house to its officers.
Value of Rent-free Unfurnished House Accommodation provided to ' Other than Government Employees ' – when the accommodation is taken on lease or rent by employer	Amount of lease rent paid or payable or 15 per cent of “Salary”, whichever is less .
Value of Rent-free Unfurnished House Accommodation provided to ' Other than Government Employees ' – when the accommodation is owned by employer	When the population of the city in which the accommodation is located (as per 2001 census) is– Exceeding 25 lakh – 15 per cent of “Salary” Exceeding 10 lakh but not exceeding 25 lakh – 10 per cent of “Salary” Not exceeding 10 lakh – 7.5 per cent of “Salary”

Notes:

- “Salary” for the purpose of valuation of rent-free accommodation includes–
 - Basic Salary
 - Taxable Portion of Allowances (Dearness Allowance must be considered only if it enters into retirement benefits)
 - Bonus
 - Any Commission
 - Dearness Pay
 - Fees
 - Taxable portion of any other monetary payment, not being a perquisite.
- “Salary” for this purpose must be calculated on ‘accrual’ basis. That is, the total of all above items belonging to the period for which the accommodation was provided to employee during previous year must be considered, irrespective of whether the items are received or not; and taxable or not.
- Where the employee is serving with more than one employer during the period for which he is provided with rent-free accommodation, the above listed items from all employers for the said period must be considered for calculating “Salary”.

Valuation of Rent-free Furnished House Accommodation

Where the accommodation provided to employee is furnished, the taxable value is calculated as follows–

Value of Rent-free Unfurnished House Accommodation (calculated as above)	XXX
Add: Value of Furniture	XXX
	XXX

Value of Furniture = Actual hire charges of furniture (if the furniture is hired by employer) or 10 per cent *per annum* of the 'original cost' of furniture (if the furniture is owned by employer).

Valuation of Hotel Accommodation provided to employee and his family

Hotel accommodation includes accommodation provided in motels, service apartments and guest house. The taxable value of this nature of accommodation provided to employee is—

Actual charges payable to Hotel by the employer;

Or

24% of "Salary"

whichever is less.

Note: "Salary" for this purpose is same as explained earlier in the case of rent-free house accommodation.

Illustration 38 Problem on valuation of rent-free accommodation

Narendra, an officer of Government of Karnataka, draws basic salary of ₹7,000 p.m. He is provided with rent-free unfurnished accommodation, fair rent of which is ₹1,800 p.m. As per Government Rules, the License Fee of the accommodation is ₹600 p.m. What is the taxable value of rent free accommodation facility provided to Narendra.

Solution:

- Mr. A is a Government employee.
- Value of unfurnished rent-free accommodation provided to him is the Licence Fee determined by the Government.

Hence, the value of rent-free unfurnished accommodation is **₹7,200** (i.e., ₹600 × 12).

Illustration 39 Problem on valuation of rent-free accommodation

Bharath, an employee of ABC Ltd., posted at Bangalore draws ₹60,000 p.a. as Basic Salary; ₹20,000 p.a. as Dearness Allowance forming part of salary and ₹5,000 as Commission. The company has provided him a rent-free unfurnished accommodation whose fair rental value is ₹32,000 p.a. Determine the value of perquisite in respect of rent-free accommodation provided to Mr. Bharat

Solution:

- Bharath is not a Government employee
- The accommodation provided to him is owned by the employer
- The accommodation is in Bangalore where the population as per 2001 census exceeds 25 Lakhs
- Salary for the purpose of valuation of rent-free unfurnished accommodation is
 - = Basic Salary + Dearness Allowance forming part of salary + Commission
 - = 60,000 + 20,000 + 5,000
 - = 85,000

- Value of rent-free unfurnished accommodation provided to Bharath is 15% of Salary.
Hence, the value of rent-free unfurnished accommodation is ₹12,750 (i.e., 85,000 × 15%).

Illustration 40 Problem on valuation of rent-free accommodation

Venugopal, an employee of PQR Ltd., draws ₹40,000 p.a. as Basic Pay, ₹6,500 p.a. as Dearness Allowance (not forming part of salary) and ₹7,000 p.a. as Bonus. He is provided with a rent-free unfurnished accommodation at Mangalore. Lease rent paid by the company in respect of this accommodation is ₹10,500 p.a. Determine the value of perquisite in respect of rent-free accommodation provided to Venugopal.

Solution:

- Venugopal is not a Government employee
- The accommodation provided to him is not owned by the employer (as the employer is paying a lease rent of ₹10,500)
- The city in which the accommodation is situated and its population is irrelevant
- Salary for the purpose of valuation of rent free unfurnished accommodation is
= Basic Salary + DA forming part of salary + Bonus
= 40,000 + Nil + 7,000
= 47,000
- Value of rent free unfurnished accommodation provided to Venugopal is lease rent or 15% of salary whichever is less
Hence, the value of rent-free unfurnished accommodation is least of the following:
(a) Lease rent paid by employer ₹10,500, or
(b) 15% of salary ₹7,050 (i.e., 47,000 × 15%) whichever is less.
₹7,050 being least of the above, is the value of rent free unfurnished accommodation provided to Venugopal.

Illustration 41 Problem on valuation of rent-free accommodation

Anuradha, an employee of XYZ Ltd., based in Mysore, draws ₹9,000 p.m. as Basic Salary. Other allowances and benefits attached to her office are as follows: Dearness Allowance entering into retirement benefits 20% of Basic Salary; Bonus 2 months Basic Salary; Commission ₹800 p.m., Income Tax of Anuradha paid by the company on her behalf ₹6,000; Salary of April and May 2018 paid in advance ₹18,000. The company pays lease rent of ₹18,000 p.a. Determine the value of perquisite in respect of rent-free accommodation provided to Anuradha.

Solution:

- Anuradha is not a Government employee
- The accommodation provided to her is not owned by the employer (as the employer is paying a lease rent of ₹18,000)
- The city in which the accommodation is situated is irrelevant

9.70 • Income Tax - I

- Salary for the purpose of valuation of rent-free unfurnished accommodation is
= Basic Salary + Dearness Allowance forming part of salary + Bonus + Commission
= $(9,000 \times 12) + (9,000 \times 12 \times 20\%) + (9,000 \times 2) + (800 \times 12)$
= 1,08,000 + 21,600 + 18,000 + 9,600
= 1,57,200
- Value of rent free unfurnished accommodation provided to Anuradha is lease rent or 15% of salary whichever is less.

Hence, the value of rent-free unfurnished accommodation is least of the following:

(a) Lease rent paid by employer ₹18,000 or

(b) 15% of salary ₹23,580 (i.e., $1,57,200 \times 15\%$) whichever is less.

₹18,000 being least of the above, is the value of rent free unfurnished accommodation provided to Anuradha.

Note: Income Tax of Anuradha paid by the company on her behalf ₹6,000 and Salary of April and May 2018 paid in advance ₹18,000 does not form part of salary for valuation of rent-free unfurnished accommodation.

Illustration 42 Problem on valuation of rent-free accommodation

Arathi is employed in Holenarasipura, a Taluk Centre where the population as per 2001 census is less than 10 Lakhs. She has drawn salary as under: Basic Salary ₹8,000 p.m., Dearness Allowance 25% of Basic (60% enters for retirement benefits); Bonus 2 months Basic; Commission ₹4,500 p.a., Entertainment Allowance ₹600 p.m. The company has provided her a rent-free accommodation fair rent of which is ₹48,000 p.a. She is also provided with furniture costing ₹40,000. Determine the value of perquisite in respect of rent-free accommodation provided to Arathi.

Solution:

- Arathi is not a Government employee
- The accommodation provided to her is owned by the employer
- The accommodation is in Holenarasipura where the population as per 2001 census is less than 10 Lakhs.
- Salary for the purpose of valuation of rent-free unfurnished accommodation is
= Basic Salary + DA forming part of salary + Bonus + Commission + Entertainment Allowance
= $(8,000 \times 12) + (8,000 \times 12 \times 25\% \times 60\%) + (8,000 \times 2) + 4,500 + (600 \times 12)$
= 96,000 + 14,400 + 16,000 + 4,500 + 7,200
= ₹1,38,100.
- Value of rent-free unfurnished accommodation provided to Arathi is 7.5% of Salary.

Hence, the value of rent-free **unfurnished** accommodation is **₹10,357.50** (i.e., $1,31,800 \times 7.5\%$).

Arathi is also provided with furniture of the value of ₹40,000. Therefore, value of rent-free **furnished** accommodation is arrived at as follows:

	₹
Value of rent-free unfurnished accommodation	10,357.50
Add: 10% of the cost of furniture provided ($40,000 \times 10\%$)	4,000.00
Taxable value of rent-free furnished accommodation	14,357.50

Illustration 43 Problem on valuation of rent-free accommodation

Manjunath is employed in Mysore where the population as per 2001 census is 15 Lakhs. He has drawn salary as under: Basic Salary ₹60,000 p.a.; Dearness Allowance ₹36,000 (50% forming part of salary); Conveyance Allowance ₹5,000 (amount spent ₹1,500); Medical Allowance ₹3,000 (amount spent ₹2,000). He is provided with rent-free accommodation fair rent of which is ₹48,000 p.a. He is also provided with furniture costing ₹25,000; Hire charges of the air conditioner installed in the house amounted to ₹3,650. Compute the Gross Salary of Manjunath.

Solution:

Computation of Gross Salary of Manjunath

	₹	₹
Basic Salary		60,000
Dearness Allowance		36,000
Conveyance Allowance	5,000	
Less: Exempt	<u>1,500</u>	3,500
Medical Allowance (Fully taxable)		3,000
Value of rent-free furnished accommodation		15,500
Gross Salary		1,18,000

Note on value of rent-free furnished accommodation:

- Manjunath is not a Government employee. (In the absence of specific information, the assessee has been assumed as other than Government employee).
- The accommodation provided to him is owned by the employer.
- The accommodation is in Mysore where the population as per 2001 census is more than 10 Lakhs but less than 25 Lakhs.
- Salary for the purpose of valuation of rent-free unfurnished accommodation is
 = Basic Salary + Dearness Allowance forming part of salary + Taxable portion of Conveyance Allowance + Medical Allowance
 = $60,000 + (36,000 \times 50\%) + 3,500 + 3,000 = \text{₹}84,500$
- Value of rent free **unfurnished** accommodation provided to Manjunath is 10% of Salary.

9.72 • Income Tax - I

Hence, the value of rent free **unfurnished** accommodation is ₹8,450 (i.e., $84,500 \times 10\%$)

Manjunath is also provided with furniture of the value of ₹25,000. Therefore, value of rent-free **furnished** accommodation is arrived at as follows:

	₹
Value of rent-free unfurnished accommodation	8,450
Add: 10% of the cost of furniture provided ($25,000 \times 10\%$)	2,500
Add: Hire charges of the air conditioner installed in the house	4,550
Taxable value of rent-free furnished accommodation	15,500

Illustration 44 Problem on valuation of rent-free accommodation

Gowrish received the following emoluments: Basic Pay ₹1,62,000; Special Allowance ₹9,000; Dearness Pay ₹36,000; Dearness Allowance 20% of Basic Pay (not forming part of salary for retirement benefits); Bonus 2 months Basic Pay; City Compensatory Allowance ₹250 p.m., Children Education Allowance ₹150 per month per child for 3 children; Uniform Allowance ₹100 p.m. (entire amount is spent for the maintenance of uniform); Lunch Allowance ₹300 p.m. (Actual lunch expenses ₹1,200 per month); He is also provided with a rent-free furnished flat, lease rent of which is ₹2,50,000 p.a. (the cost price of house hold appliances provided is ₹36,000 and hire charges paid by the company in respect of air conditioner installed in the house amounted to ₹10,000). The employer paid ₹2,000 professional tax on behalf of Gowrish. Compute the Gross Salary Income of Gowrish.

Solution:

Computation of Gross Salary of Mr. Gowrish

	₹	₹
Basic Pay		1,62,000
Special Allowance		9,000
Dearness Pay		36,000
Dearness Allowance ($₹1,62,000 \times 20\%$)		32,400
Bonus 2 months Basic Pay $\{(1,62,000/12) \times 2\}$		27,000
City Compensatory Allowance (250×12)		3,000
Children Education Allowance ($150 \times 12 \times 3$)	5,400	
Less: Exempt	<u>2,400</u>	3,000
Uniform Allowance ($₹100 \times 12$)	1,200	
Less: Exempt (amount spent)	<u>1,200</u>	Nil
Lunch Allowance ($₹300 \times 12$) (Fully Taxable)		3,600
Value of rent free furnished flat (see note below)		50,440
Professional tax paid by employer on behalf of Mr. Gowrish		2,000
Gross Salary		3,28,440

Note on value of rent-free furnished accommodation:

- Gowrish is not a Government employee
- The accommodation provided to him is not owned by the employer (as the employer is paying a lease rent of ₹2,50,000)
- The city in which the accommodation is situated and its population is irrelevant
- Salary for the purpose of valuation of rent-free unfurnished accommodation is
 = Basic Pay + Special Allowance + Dearness Pay + Dearness Allowance (entering into retirement benefits) + Bonus + CCA + Taxable portion of Children Education Allowance + Taxable Portion of Uniform Allowance + Lunch Allowance + Professional tax paid by employer on behalf of Gowrish
 = 1,62,000 + 9,000 + 36,000 + Nil + 27,000 + 3,000 + 3,000 + Nil + 3,600 + 2,000
 = 2,45,600
- Value of rent-free unfurnished accommodation provided to Gowrish is Lease rent or 15% of salary whichever is less.

Hence, the value of rent-free unfurnished accommodation is least of the following:

- (a) Lease rent paid by employer ₹2,50,000 or
- (b) 15% of salary ₹36,840 (i.e., $2,45,600 \times 15\%$) whichever is less.

₹36,840 being least of the above, is the value of rent-free unfurnished accommodation provided to Gowrish

Gowrish is also provided with house hold appliances and air conditioner. Therefore, the value of rent free **furnished** accommodation is arrived at as follows:

	₹
Value of rent-free unfurnished accommodation	36,840
Add: 10% of the cost of furniture provided ($36,000 \times 10\%$)	3,600
Add: Hire charges of the air conditioner installed in the house	10,000
Taxable value of rent free furnished accommodation	50,440

Illustration 45 Problem on valuation of rent-free accommodation

Srinivas, an employee at Kolar, receives the following from his employer during previous year 2017-18.

Basic Salary – ₹25,000 per month.

Dearness allowance – ₹15,000 per month (50% enters into retirement benefits)

Other taxable allowances – ₹5,000 per month

Commission on profits – ₹10,000

Bonus received ₹75,000 (of which ₹50,000 belongs to previous year 2016-17, and ₹25,000 pertaining to previous year 2017-18 is still outstanding)

Encashment of earned leave – ₹25,000

Medical expenses of his family reimbursed by employer – ₹12,000

Rent-free furnished accommodation.

The furniture provided includes sofa-set, dining-table and cots which are owned by the employer. These items were purchased by the employer for ₹75,000 three years back.

Further, an air-conditioner has been provided from August 2017, the cost of which paid by employer was ₹48,000.

The employer had also hired book-racks for employee's use. The rental charges were ₹500 per month.

Calculate the taxable value of rent-free accommodation in the following situations:

- Srinivas is an employee of Karnataka Government and the license fee according to Government Rules is ₹48,000 per annum.
- Srinivas is an employee of Canara Bank and the accommodation provided to him is owned by the Bank.
- Srinivas is an employee of a private college and the accommodation provided to him is leased by his college at a monthly rent of ₹5,000.
- Srinivas is an employee of a private firm and the accommodation provided to him is a service apartment, the tariff for which is ₹11,000 per month, being paid by the firm.

Note: As per 2001 census, the population of Kolar was less than 10,00,000.

Solution:

- “Salary” for the purpose of valuation of ‘rent-free accommodation’

	₹
Basic Salary ($₹25,000 \times 12$)	3,00,000
Taxable Allowances ($₹5,000 \times 12$)	60,000
Bonus [$₹75,000 (-) ₹50,000 (+) ₹25,000$]	50,000
Commission on profits	10,000
Dearness Allowance ($₹15,000 \times 12 \times 50/100$)	90,000
Encashment of earned leave	25,000
	5,35,000

Notes:

- ‘Salary’ is calculated on accrual basis. That is, only salary pertaining to previous year 2017-18 (i.e., the period for which rent-free accommodation is provided during the previous year) is considered. Hence, Bonus is considered after excluding earlier year's bonus received, but after including current year's bonus, yet to be received.
- Any commission can be considered for computing “Salary” for this purpose.
- Dearness Allowance is considered only to the extent it enters into retirement benefits.
- Leave salary is a monetary payment from employer, not being a perquisite.
- Medical reimbursement being a perquisite, is not considered in computing “Salary”.

2. Valuation of rent-free accommodation

Case (a) – when Srinivas is a Government Employee

	₹
Value of rent-free unfurnished accommodation [License Fees – ₹4,000 per month] – ₹4,000 × 12	48,000
Add: Value of Furniture	₹
Sofa-set, Dining-table and Cots (₹75,000 × 10/100)	7,500
Air-conditioner (₹48,000 × 10/100 × 8/12)	3,600
Book-racks (₹500 × 12)	6,000
	17,100
	65,100

Case (b) – Srinivas is an employee of Canara Bank and the accommodation provided to him is owned by the Bank.

	₹
Value of rent-free unfurnished accommodation	
7.5% of “Salary” (7.5/100 × ₹5,35,000)	
Since, the accommodation is owned by employer and is in Kolar, being a city whose population does not exceed 10,00,000	40,125
Add: Value of Furniture	₹
Sofa-set, Dining-table and Cots (₹75,000 × 10/100)	7,500
Air-conditioner (₹48,000 × 10/100 × 8/12)	3,600
Book-racks (₹500 × 12)	6,000
	17,100
	57,225

Case (c) – Srinivas is an employee of a private college and the accommodation provided to him is leased by his college at a monthly rent of ₹5,000.

	₹
Value of rent-free unfurnished accommodation	
Actual lease rent (₹5,000 × 12) ₹60,000	
Or	
15% of “Salary” (15/100 × ₹5,35,000) ₹80,250	
Whichever is less	60,000
Add: Value of Furniture	₹
Sofa-set, Dining-table and Cots (₹75,000 × 10/100)	7,500
Air-conditioner (₹48,000 × 10/100 × 8/12)	3,600
Book-racks (₹500 × 12)	6,000
	17,100
	77,100

Case (d) – Srinivas is an employee of a private firm and the accommodation provided to him is a service apartment, the tariff for which is ₹ 11,000 per month, being paid by the firm

	₹
Accommodation provided is in the nature of hotel accommodation. Hence, the value calculated is inclusive of value of furniture. The value of the accommodation is-	
	₹
Actual tariff payable by employer ($₹ 11,000 \times 12$)	1,32,000
Or	
24% of “Salary” ($24/100 \times ₹ 5,35,000$)	1,28,400
Whichever is less	1,28,400
	1,28,400

Accommodation Provided at Concessional Rent [Section 17(2)(ii)]

Where the employee is provided accommodation facility by his employer not free of rent, but for a nominal or concessional rent, then the benefit is taxable under section 17(2)(ii).

The taxable value of this benefit, in accordance with provisions under Income Tax Rule 3(1) is–

Value of Rent-free Accommodation minus rent charged to employee.

Where, the rent charged to employee exceeds the value of rent-free accommodation, there is no concession received by employee and hence the taxable value is ‘Nil’.

Illustration 46 Problem on valuation of accommodation provided at concessional rent

Assume in illustration forty-five, the employee was charged a rent of ₹ 3,000 per month. What is the taxable value of the benefit?

Solution:

	Case (a)	Case (b)	Case (c)	Case (d)
Value of rent-free accommodation	65,100	57,225	77,100	1,28,400
Less: rent payable by employee ($₹ 3,000 \times 12$)	36,000	36,000	36,000	36,000
Value of accommodation provided at concessional rent	29,100	21,225	41,100	92,400

Personal Obligation of employee met or reimbursed by employer [Section 17(2)(iv)]

Any obligation of employee, when met or reimbursed by employer, will be taxable under section 17(2)(iv). The **taxable value** will be the **amount met or reimbursed** by employer.

Some **examples** of benefits taxable under this clause are–

- (a) Income-tax of employee paid or reimbursed by employer.
- (b) Professional tax of employee paid or reimbursed by employer.
- (c) Personal loans of employee repaid by employer.
- (d) Life insurance premium on policy of employee paid by employer, policy being taken by employee.
- (e) Life insurance premium on policy of employee's family members, paid or reimbursed by employer.
- (f) Medical benefits extended by employer to any person other than employee or members included in 'family'.
- (g) Taxable value of medical benefit in the hands of employee, when the medical bills are in the name of employee or patient (being a part of 'family').
- (h) Premium paid by employer on personal accident insurance policy in the name of employee, policy being taken by employee.
- (i) Expenses met or reimbursed by employer towards running and maintenance of motor car owned by employee and used by him for his personal purposes.
- (j) Salary paid by employer to domestic servants of employee, servants being appointed by employee.
- (k) Gas, electricity and water bills of employee paid by employer, when the connections are not in the name of employer.
- (l) Education expenses of employee's children or 'members of the household' met or reimbursed by the employer, when the children or 'members of the household' are getting educated in an institution not run by employer and the receipt is issued in the name of employee or the student etc.

Insurance premium paid by employer on life insurance policy of employee, policy being taken by employer [Section 17(2)(v)]

Any premium paid by employer on life insurance policy in the name of employee is taxable under this clause, provided the policy is taken by the employer, on employee's name.

The **amount of premium paid** by employer during the relevant previous year is the ***taxable value***.

Free or concessional allotment of shares under Employee Stock Option Plan or Sweat Equity Shares [Section 17(2)(vi)]

Where the employee is allotted shares of the company under Employee Stock Option Plan or as Sweat Equity Shares, either free of cost or at concessional rate, the benefit so received by employee is taxable under this clause. '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 know-how or making available rights in the nature of intellectual property rights or value additions, by whatever name called.

The tax treatment for this facility is provided in Income Tax Rule 3(8) and 3(9) and accordingly, the taxable value is—

Taxable Value = Fair Market Value of the specified security or sweat equity shares on the *date of exercising of the option minus* amount, if any, paid by or recovered from employee.

Determination of Fair Market Value:

	Situations	How fair market value is determined?
Case I	On the date of exercise of option the share in the company is listed on a recognized stock exchange in India.	The fair market value shall be the average of the opening price and the closing price of the share on that date on the said exchange.
Case II	On the date of exercise of option the share in the company is listed on more than one recognized stock exchange in India	The fair market value shall be the average of the opening price and closing price of the share on that date on the recognized stock exchange which records the highest volume of trading in the share.
Case III	On the date of exercise of option the share in the company is listed but there is no trading of the share on any recognized stock exchange in India	The fair market value shall be: (a) The closing price of the share on any recognized stock exchange on a date closest to the date of exercise of the option and immediately preceding such date; or (b) The closing price of the share on any recognized stock exchange, which records the highest volume of trading in the share, if the closing price, on a date closest to the date of exercise of the option and immediately preceding such date, is recorded on more than one recognized stock exchange.
Case IV	On the date of exercise of option the share in the company is not listed on a recognized stock exchange (including a case where share is listed abroad but not on any recognized stock exchange in India)	The fair market value shall be such value of the share of the company as determined by a merchant banker on the specified date. 'Specified date' means (i) the date of exercise of the option; or (ii) any date earlier than the date of exercising the option, not being a date which is more than 180 days earlier than the date of option. (‘Merchant banker’ means Category I merchant banker registered with Securities and Exchange Board of India)

Illustration 47 Problem on Valuation of Sweat Equity Shares

AB Co Ltd. allotted 1000 Sweat Equity Shares to Sri Chand in June 2017. The shares were allotted at ₹200 per share. On the date of exercise of the option by the allotted viz., Sri Chand, the shares of the company had an opening price of ₹325 and closing price of ₹380. The fair market value was computed in accordance with the method prescribed under the Act. What is the perquisite value of Sweat Equity Shares allotted to Sri Chand?

Solution:

Taxable Value = **Fair Market Value** of the specified security or sweat equity shares on the *date of exercising of the option* **minus** amount, if any, paid by or recovered from employee.

Fair market value = Average of opening price and closing price on the date of exercise of option
 $= (\text{₹}325 + \text{₹}380)/2 = \text{₹}352.50$.

Taxable value = $(\text{₹}352.50 - \text{₹}200) \times 1000 \text{ shares} = \text{₹}1,52,500$.

Contribution by employer to employee's approved superannuation fund [Section 17(2)(vii)]

Any contribution made by employer towards approved superannuation fund account in the name of employee is taxable under this clause, to the extent the contribution during the relevant previous year exceeds ₹1,00,000.

Other Fringe Benefits [Section 17(2)(viii)]

'Fringe Benefits' refer to other peripheral benefits given to employee, in accordance with employer's policy. These benefits may not relate to the office or position of the employee, but are generally available to all employees of an organisation.

'Fringe Benefits' under the above mentioned clause includes—

- Interest free or concessional interest loan advanced to employee
- Holiday-home facility
- Free or concessional food and non-alcoholic beverage
- Gifts
- Credit card facility
- Club facility
- Free or concessional use of employer's movable asset
- Transfer of any movable asset by employer.

A detailed discussion of the tax provisions pertaining to above benefits, is made in the following paragraphs:

The term 'members of the household of the employee', used in the following provisions include—

- (i) Spouse of the employee,
- (ii) Children of the employee and their spouses,
- (iii) Parents of the employee,
- (iv) Servants of the employee and their dependents.

Interest free or concessional interest loan advanced by employer to employee or any member of the household of the employee

When an interest-free or concessional interest loan is advanced by employer to employee or any 'member of the household of the employee', the amount of interest saved on account of borrowing from employer, is the benefit to employee. Where the same amount of loan was borrowed by

employee from another source, he would have paid interest. But, having borrowed from employer free of interest or at nominal interest, he is saving interest. It is a benefit to the employee and hence taxed as a perquisite.

The taxable value of this benefit, in accordance with Income Tax Rule 3(7)(i), is calculated as follows—

Maximum Outstanding Monthly Balance × Rate of interest charged by

SBI on the first day of the relevant previous year	XXX
Less: Interest amount, if any, recovered from employee	XXX
	XXX

Notes:

- 'Maximum outstanding monthly balance' refers to the outstanding balance of each loan as on the **last day of each month**.
- The rates of interest charged by the State Bank of India, as on 1st April 2017 (applicable to previous year 2017-18) are as follows:

Type of Loan	Tenure or Terms	Rate of Interest (%)
Housing Loan	For Women borrowers	8.60
	Others	8.65
Car Loan	For Women borrowers	9.20
	Others	9.25
	Certified pre-owned cars (for all borrowers)	12.65
Two Wheeler Loan		11.65
Education Loan	Up to ₹7.5 lakhs	10.00
	Above ₹7.5 lakhs	10.75
	Note: Concession of 0.5% for Girl students	
Personal Loan		12.65 – 15

Note: For tax purposes, the rate of interest as charged by SBI on 1st April 2017 must be considered, and not the rate of interest as on the date of advancing the loan by employer.

Cases where interest-free or concessional interest loan is not taxable are given under 'tax-free perquisites' – (Item No. 2)

Illustration 48 Problem on computing taxable value of 'interest-free loan' benefit

Vittam Ltd., advanced an interest-free loan of ₹8,00,000 to its marketing manager Meera for purchase of a car, in the month of August 2017. What is the taxable value of the benefit, if Meera is repaying ₹25,000

- On the first of each month.
- On the last day of each month.

Solution:

The rate of interest for a car loan on 1st April 2017, as charged by SBI was 9.20%. The savings in interest to employee is calculated at that rate.

Situation 1: When the re-payments are made on the first of each month:

Month	Maximum outstanding monthly balance (₹)	Interest Calculation	Amount of Interest (₹)
August 2017	8,00,000	₹8,00,000 × 9.20/100 × 1/12	6133.33
September 2017	7,75,000	₹7,75,000 × 9.20/100 × 1/12	5941.67
October 2017	7,50,000	₹7,50,000 × 9.20/100 × 1/12	5750.00
November 2017	7,25,000	₹7,25,000 × 9.20/100 × 1/12	5558.33
December 2017	7,00,000	₹7,00,000 × 9.20/100 × 1/12	5366.67
January 2018	6,75,000	₹6,75,000 × 9.20/100 × 1/12	5175.00
February 2018	6,50,000	₹6,50,000 × 9.20/100 × 1/12	4983.33
March 2018	6,25,000	₹6,25,000 × 9.20/100 × 1/12	4791.67
Total	57,00,000		43,700.00

Notes:

- (a) Since the re-payments are made on the first of each month, the first re-payment will be on 1st September 2017. Hence, for the month of August 2017, the maximum outstanding balance is ₹8,00,000. From the following month, the maximum outstanding balance on the last day will be ₹25,000 less than that of the previous month.
- (b) The amount of interest saved by employee can also be calculated as follows—
Total outstanding balance for the relevant previous year × Rate/100 × 1/12
- (c) That is, (₹57,00,000 × 9.20/100 × 1/12) = ₹43,700.00.

Situation 2: When the re-payments are made on the last day of each month:

Month	Maximum outstanding monthly balance (₹)	Interest Calculation	Amount of Interest (₹)
August 2017	7,75,000	₹7,75,000 × 9.20/100 × 1/12	5941.67
September 2017	7,50,000	₹7,50,000 × 9.20/100 × 1/12	5750.00
October 2017	7,25,000	₹7,25,000 × 9.20/100 × 1/12	5558.33
November 2017	7,00,000	₹7,00,000 × 9.20/100 × 1/12	5366.67
December 2017	6,75,000	₹6,75,000 × 9.20/100 × 1/12	5175.00
January 2018	6,50,000	₹6,50,000 × 9.20/100 × 1/12	4983.33
February 2018	6,25,000	₹6,25,000 × 9.20/100 × 1/12	4791.67
March 2018	6,00,000	₹6,00,000 × 9.20/100 × 1/12	4600.00
Total	55,00,000		42,166.67

Notes:

- (a) Since the re-payments are made on the last day of each month, the first re-payment will be on the last day of August 2017. Hence, for the month of August 2017, the maximum outstanding balance is ₹7,75,000.
- (b) The amount of interest saved by employee can also be calculated as follows:
Total outstanding balance for the relevant previous year \times Rate/100 \times 1/12
 That is, $(₹55,00,000 \times 9.20/100 \times 1/12) = ₹42,166.67$.
- (c) That taxable value of the perquisite can be rounded off to nearest rupee and taken as **₹42,167**.

Illustration 49 Problem on computing taxable value of 'concessional interest loan' benefit

Suppose in Illustration Number Forty-Eight, employer charged interest at the rate of 6.5% per annum, what would be the taxable value of the benefit?

Solution:

The taxable value of the benefit would be—

Total outstanding balance for the relevant previous year \times Rate/100 \times 1/12

Situation 1: $₹57,00,000 \times (9.20 - 6.50)/100 \times 1/12 = ₹12,825$

Situation 2: $₹55,00,000 \times (9.20 - 6.50)/100 \times 1/12 = ₹12,375$

Illustration 50 Problem on computing taxable value of 'concessional interest loan' benefit

Ved Software Ltd. has granted to one of its employees Badri, a housing loan @ 6% per annum. The loan amount outstanding on 1st April 2017 is ₹6,00,000. Mr. Badri pays ₹12,000 on the 5th of each month towards principal amount. Calculate the taxable value of the benefit in the hands of Mr. Badri.

Solution:

Mr. Badri has borrowed a loan from his employer at a concessional rate. The concession in the interest is the benefit to him and is taxable as perquisite.

The rate of interest on housing loan charged by SBI as on 1st April 2017 was 8.65%.

For calculating taxable value, the maximum outstanding monthly balance is ascertained as follows—

Month	Maximum Outstanding Monthly Balance (₹)
April 2017	5,88,000
May 2017	5,76,000
June 2017	5,64,000
July 2017	5,52,000
August 2017	5,40,000
September 2017	5,28,000

Month	Maximum Outstanding Monthly Balance (₹)
October 2017	5,16,000
November 2017	5,04,000
December 2017	4,92,000
January 2018	4,80,000
February 2018	4,68,000
March 2018	4,56,000
Total	62,64,000

The taxable value of the benefit for Badri for previous year 2017-18 is–

$$₹62,64,000 \times (8.65 - 6)/100 \times 1/12 = ₹13,833.$$

Holiday Home Facility

Where employee or ‘members of the household’ of employee are provided accommodation facility while on holiday, and/or any other expenses incurred by employee or ‘members of the household’ of the employee during holiday or vacation are met or reimbursed by employer, the benefit, which is personal in nature, is taxable as perquisite.

The taxable amount of this benefit must be calculated as follows, in accordance with Income Tax Rule 3(7)(ii)–

Situation	Taxable Value
Where the holiday home facility belongs to employer and is made available to all employees uniformly	Expenditure incurred by the employer <i>minus</i> any amount recovered from employee.
Where the holiday home facility belongs to employer and not made available uniformly to all employees	Value at which such facilities are offered by other agencies to the public <i>minus</i> any amount recovered from employee
Where the holiday home facility does not belong to employer	Amount of expenditure met or reimbursed by employer <i>minus</i> any amount recovered from employee.

Free or Concessional Food and Non-alcoholic Beverages

Where employer provides facility of food and beverages to employees either in office premises, or through non-transferrable paid vouchers usable at eating joints, the employee is benefited when there is no charge for the facility or is charged nominally. The taxable value of this benefit, in accordance with Income Tax Rule 3(7)(iii), is calculated as follows–

Cost to employer in excess of ₹50 per meal	XXX
Less: Any amount recovered from employee	XXX
	XXX

Cases where free or concessional food facility is not taxable are given under 'tax-free perquisites' – (Item No. 3)

Illustration 51 Problem on computing taxable value of free or concessional food facility

Dayanand Ltd. provides its employees with lunch on all working days, through a caterer who charges ₹125 per meal. The company works for 5 days a week. What is the taxable value of the benefit to Mr. Sreekanth, an employee of the company for previous year 2017-18 if–

- The company provides lunch free of cost.
- The company charges each employee ₹35 per meal.

Solution:

At the rate of 5 working days per week, the total working days in a year is 260 (52×5).

Situation 1: When lunch is provided free of cost

The taxable value in this case is–

(₹125 per meal – ₹50) per meal \times 260 days = ₹19,500.

Situation 2: When lunch is provided at concessional rate

The taxable value in this case is–

$[(₹125 - ₹50) \text{ per meal} - ₹35 \text{ per meal}] \times 260 \text{ days} = ₹10,400.$

Gifts

Where employer provides gifts to employees, they are taxable as perquisites under 'fringe benefits'. The gifts given may be for personal or official reasons. The tax provisions for this benefit, in accordance with Income Tax Rule 3(7)(iv), are as under–

Situation	Taxable Value
Where the gifts are given in monetary form (i.e., in cash, by cheque, bank transfer, etc.)	The aggregate value of ' cash gift ' received by employee during previous year is fully taxable .
Where the gifts are given in non-monetary forms like gift vouchers, mementos, articles, valuables, etc.	The aggregate value of 'gifts-in-kind' received by employee during previous year, to the extent it exceeds ₹5,000, is taxable. (That is, where the aggregate value of 'gifts in kind' is less than or equal to ₹5,000, it is tax-free, and when the aggregate value exceeds ₹5,000, the excess value over and above ₹5,000 is taxable.)

Credit Card Facility

Where the employer provides credit card to employee or any 'member of the household' of the employee, the expenditure incurred by employer to provide such facility is taxable in the hands of employee as 'fringe benefits'.

The taxable value of this facility, in accordance with Income Tax Rule 3(7)(v), is calculated as under–

Expenditure incurred by employer in respect of credit card used by employee or any member of his household (excluding usage for official purposes)	XXX
Less: any amount recovered from employee	XXX
	XXX

Note: Only expenditure incurred by employer to provide credit card facility like membership fees, annual fees, etc., is taxable. Credit card bills of employee met or reimbursed by employer is taxable as ‘*personal obligation of employee met or reimbursed by employer*’ under section 17(2)(iv) to the extent the bill amount pertains to personal use of employee.

Case where credit card facility is not taxable is given under ‘tax-free perquisites’ – (Item No. 5)

Club Facility

Where the employer provides membership of any club to employee of any ‘member of the household of employee’, the benefit is taxable as perquisite in the hands of the employee.

The taxable value of this facility, in accordance with Income Tax Rule 3(7)(vi), is calculated as under–

Expenditure incurred by employer in respect of club facility for use of employee Or any member of his household (excluding usage for official purposes)	XXX
Less: any amount recovered from employee	XXX
	XXX

Note: Only expenditure incurred by employer to provide club membership is taxable. Club bills met or reimbursed by employer is taxable as ‘*personal obligation of employee met or reimbursed by employer*’ under section 17(2)(iv) to the extent the bill amount pertains to personal use of employee.

Cases where club facility is not taxable are given under ‘tax-free perquisites’ – (Item No. 6)

Free or Concessional Use of Employer’s Movable Assets

Where an employee of any ‘member of the household’ of employee uses any movable asset provided by employer (*other than computers, lap tops, mobile phones, telephone and motor-car*) for their personal purpose, either without making any payment, or for a nominal charge, then the benefit is taxable as perquisite.

The taxable value of this benefit, in accordance with Income Tax Rule 3(7)(vii), is calculated as under:

Value of the Movable Asset	XXX
Less: any amount recovered from employee	XXX
	XXX

Value of the Asset

- (i) Where the asset is hired by employer – Actual Hire Charges
- (ii) Where the asset is owned by employer – 10% *per annum* of the ‘Original Cost’ of the Asset.

Note: For motor car provided by employer to employee, there are separate valuation provisions given under Income Tax Rules. Hence, it is not considered here.

Illustration 52 Problem on tax treatment of use of employer’s movable assets by employee

Explain the tax-treatment for the following benefits received by Satish from his employer RCC Ltd.

1. Satish is given a lap top by his company, which is used by him for both official and personal purposes. The cost of lap top was ₹60,000 and the ownership is not transferred.
2. The company has provided a mobile phone to Satish which is used by him for both official and personal purposes. The cost of the phone was ₹25,000 and the mobile bills paid by company during previous year were ₹15,000.
3. Satish had used Sony Video Camera of his company during his personal tour to Malaysia and for a ceremony at home. The cost of Camera to the company was ₹2,40,000. It was used by Satish for 45 days during previous year 2017-18 and the company charged him ₹1,500 for the usage.
4. The company had hired a music system and given it to personal use of Satish. The hire charges were ₹500 per month. It was used by Satish for 8 months during previous year 2017-18. The company did not charge any consideration to Satish, for the use of music system.
5. Furniture costing ₹1,00,000 was given by the Company, for use of Satish at his residence. It was used by Satish for entire period of relevant previous year.

Solution:

The tax treatment in each of the above case is shown in the following table:

Case Number	Transaction	Tax Treatment
Case 1	Satish is given a lap top by his company, which is used by him for both official and personal purposes. The cost of lap top was ₹60,000 and the ownership is not transferred.	Use of employer’s lap top by employee is not taxable , irrespective of the purpose of its usage.

Case Number	Transaction	Tax Treatment
Case 2	The company has provided a mobile phone to Satish which is used by him for both official and personal purposes. The cost of the phone was ₹25,000 and the mobile bills paid by company during previous year were ₹15,000.	Mobile phone facility provided by employer to employee is not taxable , irrespective of the purpose of its usage. Where, the mobile phone is not provided by employer, but the bills are paid by employer. Then, to the extent the phone was used by employee for personal purpose, the bill paid by employer is taxable as 'personal obligation of employee met or reimbursed by employer under section 17(2)(iv)'.
Case 3	Satish had used Sony Video Camera of his company during his personal tour to Malaysia and for a ceremony at home. The cost of Camera to the company was ₹2,40,000. It was used by Satish for 45 days during previous year 2017-18 and the company charged him ₹1,500 for the usage.	This benefit is taxable as 'fringe benefit'. The taxable value of this benefit is— $(₹2,40,000 \times 10/100 \times 45/365) - ₹1,500 = ₹2,959 (-) ₹1,500 = ₹1,459.$ Since, the asset used by employee belongs to employer, the value is taken as 10% per annum of the 'original cost' of the asset.
Case 4	The company had hired a music system and given it to personal use of Satish. The hire charges were ₹500 per month. It was used by Satish for 8 months during previous year 2017-18. The company did not charge any consideration to Satish, for the use of music system.	This benefit is taxable as 'fringe benefit'. The taxable value of this benefit is— $(₹500 \times 8) = ₹4,000.$
Case 5	Furniture costing ₹1,00,000 was given by the Company, for use of Satish at his residence. It was used by Satish for entire period of relevant previous year.	Where the furniture is provided to the employee, along with accommodation, then the value of furniture must be considered while calculating the value of 'rent-free accommodation'. The value of furniture that must be added in arriving at taxable value of 'rent-free accommodation' is— $(₹1,00,000 \times 10/100) = ₹10,000.$ Where the furniture is provided to the employee independently, without providing any accommodation facility, then the value of furniture must be charged under 'fringe benefits'. The taxable value of this benefit is— $(₹1,00,000 \times 10/100) = ₹10,000.$

Transfer of Employer's movable assets to employee

Where an employer transfers any movable asset owned by him to any employee or any 'member of the household' of the employee without consideration or for a nominal consideration, then the benefit is taxable in the hands of the employee, as a perquisite.

The taxable value of this benefit, in accordance with Income Tax Rule 3(7)(viii), is calculated as under—

Original Cost of the Asset	XXX
Less: Normal wear and tear for each completed year of life	XXX
	XXX
Less: Any consideration paid by employee	XXX
	XXX

Notes:

The deduction for 'Normal Wear and Tear' must be calculated at the following rates:

Asset	Rate of Normal Wear and Tear
Computers and electronic items (i.e., data storage devices)	50% of 'reduced balance'
Motor Cars	20% of 'reduced balance'
Other Assets	10% of 'original cost'

The deduction for normal wear and tear must be provided for each completed year of life of the asset. Suppose, the employer purchased an asset in May 2013 and transferred the same to an employee in January 2018. Till the date of transfer, the asset is used by employer for 3 years and 9 months. However, deduction for normal wear and tear must be provided only for completed years, which is 3 years in this case.

Illustration 53 Problem on Computation of Taxable Value of certain fringe benefits

GRCC Ltd. transferred the following assets used by it, to its employee Govindappa on **1st February, 2018**. The required details of the assets transferred are given below. Calculate the taxable value of benefits, if any:

Particulars	Laptop	Motor Car	Air-conditioner	Refrigerator
Date of purchase by employer	1/8/2014	1/9/2015	21/3/2014	18/6/2016
Original cost of the asset	₹96,000	₹8,00,000	₹48,000	₹30,000
Consideration payable by Govindappa	₹10,000	₹3,00,000	Nil	₹28,000

Solution:

Transfer of movable assets of employer to employee, free of cost or for nominal consideration, is a benefit to employee, taxable as 'fringe benefit'.

The taxable value of the assets transferred is calculated as follows:

Particulars	Laptop	Motor Car	Air-conditioner	Refrigerator
Period for which asset was used by employer (i.e., duration between date of acquisition by employer and date of transfer to employee)	3 Years and 6 Months	2 Years and 5 Months	2 Years, 10 Months and 10 Days	1 Year, 7 Months and 13 Days
No. of Completed Years	3	2	2	1
Rate of Normal Wear and Tear	50% of 'reduced balance'	20% of 'reduced balance'	10% of 'original cost'	10% of 'original cost'
Value of the asset at the time of its transfer to employee	₹	₹	₹	₹
Original Cost:	96,000	8,00,000	48,000	30,000
Less: Normal wear and tear for first completed year	48,000	1,60,000	4,800	3,000
	48,000	6,40,000	43,200	27,000
Less: Normal wear and tear for second completed year	24,000	1,28,000	4,800	
	24,000	5,12,000	38,400	
Less: Normal wear and tear for third completed year	12,000			
	12,000			
Less: Consideration payable by employee	10,000	3,00,000	Nil	28,000
Taxable Value	2,000	2,12,000	38,400	Nil

Notes:

- Normal wear and tear must be provided only for completed years of usage of asset by employer. (This is on par with the provision of depreciation under section 32).
- Air-conditioner is transferred to employee without consideration. Hence, it amounts to gift in kind. The aggregate value of 'gifts in kind' received by employee during relevant previous year is tax-free up to ₹5,000 and only the excess amount is taxable. So, in this case, the taxable value of transfer of air-conditioner is ₹33,400 (i.e., ₹38,400 minus ₹5,000).
- Where the consideration payable by employee exceeds the value of the asset on the date of its transfer, there is no benefit to employee and hence the taxable value is 'Nil'. 'Negative value' of an asset does not carry any meaning.

- (d) The total taxable value of this benefit in the hands of employee is ₹2,47,400 (i.e., ₹2,000 + ₹2,12,000 + ₹33,400 + Nil).

9.10.3 Perquisites Taxable in the Hands of 'Specified Employees' Only

Apart from 'tax-free perquisites' and 'perquisites taxable in the hands of all employees', any other perquisite given by employer to employee will be taxable, only when the employee is regarded as a 'specified employee'.

According to Section 17(2)(iii) of the Act, an employee is a specified employee, when

- (i) he is a **director** of the company, **or**
- (ii) he has **substantial interest** in the company, **or**
- (iii) his **total taxable monetary emoluments** from all employers during relevant previous year, after providing for deductions under section 16, **exceeds ₹50,000**.

Notes:

1. An employee can be considered as 'specified employee' when he **fulfills any one** of the above three criterion, for the relevant previous year.
2. The first criteria of 'being a director of the company' is said to be fulfilled when the employee is a director for any part of the year. Further, he can be director in any capacity – by shareholding, by nomination, etc.
3. A person is said to be having 'substantial interest' in a company when he is the 'beneficial owner' of at least 20% of equity share capital of the company. It must be noted that the employee need not be the actual owner or registered owner, but must be beneficial owner.
4. In ascertaining the fulfillment of the third criteria, the following points must be kept in mind:
 - (i) The Monetary payments or emoluments received only must be considered, and any benefit or emolument which is non-monetary must be ignored.
 - (ii) The taxable amount of those monetary benefits must be considered.
 - (iii) The total taxable amount of the monetary benefits received by employee during relevant previous year must be considered, irrespective of the number of employers from which such benefits are received.
 - (iv) From such total taxable monetary receipts, deductions under section 16 must be provided.
 - (v) The balance amount after providing for deductions under section 16 must **exceed ₹50,000**. Where the balance is ₹50,000 or less, the condition is not considered as fulfilled'.
5. The first two criteria are applicable only for employees working in corporate entities. Generally, the last criterion is applicable to all employees.

List of perquisites taxable in the hands of specified employees only

The following is the list of ‘other perquisites’ which are taxable only if the employee is a specified employee.

1. Free or concessional Motor Car Facility
2. Free or concessional conveyance facility (other than Motor Car)
3. Free or concessional facility of domestic servants.
4. Free or concessional supply of gas, electricity and water.
5. Free or concessional educational facility to ‘members of the household’ of the employee.
6. Free or concessional transport facility provided by a transport undertaking to the employee or ‘members of the household’ of its employees.
7. Any other facility not covered earlier.

A detailed discussion of the tax-treatment for the above perquisites is given below:

Motor Car Facility

Motor-car Facility may be provided by employer to employee in two different ways, viz.,

- A. Employer provides motor car to employee, and may also meet running and maintenance expenses.
- B. Employer meets or reimburses the running and maintenance expenses of the motor car which belongs to employee.

The tax provisions relating to ‘motor-car facility’, in accordance with Income Tax Rule 3(2), are summarised in the following table:

Situation	Usage of Car	Taxable Under Section	Taxable Value
Car provided by employer	Only for official purpose	Not Taxable	Nil
Car provided by employer and running & maintenance expenses met by employer	Used only for personal purposes	17(2)(iii)	Value of the Car (See Note Below) plus Running and Maintenance Expenses met or reimbursed by employer minus any amount charged to employee
Car provided by employer and running & maintenance expenses met by employee	Used only for personal purposes	17(2)(iii)	Value of the Car (See Note Below) minus any amount charged to employee
Car provided by employer and running & maintenance expenses met by employer	Used for both official and personal purposes	17(2)(iii)	Standard Value (See Note Below)
Car provided by employer and running & maintenance expenses met by employee	Used for both official and personal purposes	17(2)(iii)	Standard Value (See Note Below)

Situation	Usage of Car	Taxable Under Section	Taxable Value
Car is owned by employee and expenses are met by employer	Used for only personal purposes	17(2)(iv)	Running and maintenance expenses met or reimbursed by employer
Car is owned by employee and expenses are met by employer	Used for both official and personal purposes	17(2)(iv)	Running and maintenance expenses met or reimbursed by employer <i>minus</i> Standard Value (See Note Below)
Car is owned by employee and expenses are met by employee	Any purpose	Not a perquisite	

Cases where motor car facility is not taxable are given under 'tax-free perquisites' – (Item No. 8)

Notes:

1. “**Value of the Car**” in the above table means—
Actual hire charges for the car, if the car is hired by employer,
Or
10% per annum of the ‘original cost’ of the car, if the car is owned by employer
2. When the **car provided by employer** to employee is used by employee for **both official and personal purposes**, then the taxable value of car facility will be the ‘standard value’ as summarised in the table below:

Type of Car	Running and Expenses met by-	
	Employer	Employee
Small Car (Cubic Capacity of the engine of the Car is Less than or Equal to 1.6 Litres Or Horse Power of the car is Less than or Equal to 16)	₹ 1800 per calendar month	₹ 600 per calendar month
Big Car (Cubic Capacity of the engine of the Car exceeds 1.6 Litres Or Horse Power of the car exceeds 16)	₹ 2400 per calendar month	₹ 900 per calendar month

Note: Where free services of driver is also made available to employee (i.e., where the salary of driver is paid by employer), **₹900 per calendar month** must be added for all the values in the above table.

3. The values given in the table above is per **calendar month**, which means only 'completed calendar months' must be considered for computing taxable value. For example, where an employee is provided motor car by his employer for 5 months and 20 days, the taxable value must be calculated only for 5 months and part of a month must be ignored.
4. When **standard value is taken as 'taxable value'** of the car facility, any **amount charged to employee** for usage of the car **must not be deducted**.
5. Where the **car belongs to employee** and expenses are met or reimbursed by employer, then to the extent the car is used for **personal purposes**, the benefit becomes 'personal obligation of employee met or reimbursed by employer', and hence is taxable under section 17(2)(iv).
6. Where the **car which belongs to employee** is used by him for both **official and personal purposes**, expenses for which are met or reimbursed by employer, the tax treatment is as follows—
 - (i) If the *log book for the use of car is maintained*, then the amount of expenditure met or reimbursed by employer proportionate to personal use of car must be taken as 'taxable value'.
 - (ii) If the *log book for the use of car is not maintained*, then a **deduction** must be given from amount of expenditure met or reimbursed by employer, for arriving at taxable value. The deduction is for the extent to which the car is used for official purpose. Since, log book is not maintained, **standard value must be deducted**. For this purpose, standard value is ₹1,800 per month (in case of small car) or ₹2,400 per month (in case of big car) **Plus** ₹900 per month (in case of free services of driver).
7. Where the employee is provided different cars from a '**pool of cars**' of the employer, the taxable value can be calculated presuming only small car is provided. This assumption is for the benefit of the assessee.
8. Where an employee is provided by his employer with **more than one car** and all of them are used by him for both official and personal purposes, then for tax purposes, only one among them will be taxed as used for both purposes and the remaining cars will be taxed as if they are used for personal purposes only.

Illustration 54 Problem on tax treatment for Motor Car Facility

Find out the taxable value of the perquisite in respect of car in the following different situations for the assessment year 2018-19. The employees are specified employees in all cases

Situation 1:

X is employed by a company. He has been provided a car (1300cc) owned by the employer, cost of the car is ₹6,34,000. The expenditure incurred by the company on maintenance of the car are – petrol: ₹80,000, driver: ₹72,000 and maintenance: ₹5,000. The car can be used by X partly for official purposes and partly for private purposes. A sum of ₹12,000 is recovered from X.

Solution:

The car is provided by employer. Hence, it is taxable in the hands of employee only if he is a 'specified employee' under section 17(2)(iii).

Since, the car is used for both official and personal purposes, **standard value** must be considered as 'taxable value'. The car provided is a small car and running & maintenance expenses are met by employer. Further, driver's salary is also paid by employer, indicating that employee is provided free services of driver.

So, Taxable value = $(₹1800 + ₹900) \times 12 = ₹32,400$

Note: When standard value is taken as taxable value, no deduction must be provided for any amount charged to employee, for the use of motor car.

Situation 2:

Assume in case (a), the car is used only for private purposes. What is the taxable value of the car?

Solution:

The car is provided by employer. Hence, it is taxable in the hands of employee only if he is a 'specified employee' under section 17(2)(iii).

Since, the car is used only for private purposes, the taxable value is calculated in the following manner:

	₹	₹
Value of the Car ($₹6,34,000 \times 10/100$)		63,400
Add: Running and Maintenance Expenses incurred by Employer		
Petrol	80,000	
Driver's Salary	72,000	
Maintenance	5,000	1,57,000
		2,20,400
Less: Amount recovered from employee		12,000
		2,08,400

Situation 3:

A car (1800cc) is owned by the employer (cost of the car being ₹5,40,000). X, an employee, can use it partly for official purposes and partly for private purposes. Expenses for private purposes are, however, incurred by X. During the previous year 2016-17, the total expenditure incurred by X is ₹78,000 on car and ₹36,000 on driver.

Solution:

The car is provided by employer. Hence, it is taxable in the hands of employee only if he is a 'specified employee' under section 17(2)(iii).

Since, the car is used for both official and personal purposes, **standard value** must be considered as 'taxable value'. The car provided is a big car and running & maintenance expenses are met by employee.

So, Taxable value = ₹900 × 12 = ₹10,800

Situation 4:

Assume in situation (c) that the car can be used only for private purposes.

Solution:

The car is provided by employer. Hence, it is taxable in the hands of employee only if he is a 'specified employee' under section 17(2)(iii).

Since, the car is used only for private purposes, and expenses are met by employee, the taxable value is calculated in the following manner:

Taxable Value of the Car = ₹5,40,000 × 10/100 = ₹54,000.

Situation 5:

X owns a car (1200cc). He uses it partly for official purposes and partly for private purposes. During the previous year 2016-17, he incurs a sum of ₹60,000 on running and maintenance of car. Besides, he had engaged a driver (salary of ₹36,000). The employer reimburses the entire expenditure of ₹96,000. Logbook of the car is not maintained.

Solution:

The car is owned by employee, and the expenses are met by employee, but reimbursed by employer. Hence, the benefit if any, is taxable as 'personal obligation of employee met by employer' under section 17(2)(iv).

Since, the car is used for both official and personal purposes and logbook of the car is not maintained, the taxable value of the car is calculated in the following manner:

Taxable Value = Expenses met or reimbursed by employer **minus** Standard Valuation

So, Taxable Value = ₹96,000 – [(₹1,800 + ₹900) × 12]
 = ₹96,000 – ₹32,400
 = ₹63,600.

Note: The car is a 'small car' and employee is getting free services of driver, since driver is also reimbursed by employer.

Situation 6:

Assume that in situation (e) that the logbook of the car is maintained and 70 per cent of the expenditure is attributable towards the official use of the car. The employer to this effect gives a certificate.

Solution:

The car is owned by employee, and the expenses are met by employee, but reimbursed by employer. Hence, the benefit if any, is taxable as 'personal obligation of employee met by employer' under section 17(2)(iv).

Since, the car is used for both official and personal purposes and logbook of the car is maintained, the taxable value of the car is calculated in the following manner:

Taxable Value = Expenses met or reimbursed by employer **minus** expenditure proportionate to official use of car.

So, Taxable Value = ₹96,000 **minus** (70% of ₹96,000) = ₹28,800.

Situation 7:

A car (1700cc) is owned by the employer. All expenses (₹56,000) are incurred by the employer. The employer maintains logbook of the car. X, an employee, uses the car only for official purposes. The employer gives a certificate that the car is used only for official purposes.

Solution:

The car is provided by employer and is used by employee only for official purposes. Since, the requisite conditions for the same has been fulfilled, the car facility is **not taxable** in the hands of employee.

Illustration 55 **Problem on computing taxable value of Motor Car Facility, when more than one car is provided**

X is employed by X Ltd. He holds 14 per cent equity share capital and 50 per cent preference share capital in the company. Remaining shares in X Ltd., are owned by the relatives of X. X is not a director in X Ltd., he has been provided three cars for official and personal use. These cars cannot be used by any other employee of the company. The company incurs the following expenses in respect of these cars:

	Car 1 (1800cc) ₹	Car 2 (1200cc) ₹	Car 3 (1600cc) ₹
Petrol Bills	40,500	60,600	38,500
Maintenance expenses	8,100	7,800	9,200
Insurance	6,700	6,300	4,900
Salary of driver	24,000	—	—

Cost of cars to the employer is: ₹4,89,000, ₹5,10,000 and ₹3,50,000. Find out the value of the perquisite for the assessment year 2018-19 in respect of cars if monetary emoluments of X are (a) ₹50,000, or (b) more than ₹50,000.

Solution:

Motor Cars are provided by employer and hence taxable in the hands of employee only if he is a 'specified employee'.

Case (a):

X is neither a director in the company, nor is having substantial interest in the company. Further, the taxable value of monetary emoluments for the previous year 2016-17 is not exceeding ₹50,000. Hence, X is not a specified employee. **Therefore, the motor-car facility is not taxable in this case.**

Case (b):

X is neither a director in the company, nor is having substantial interest in the company. However, his taxable monetary emoluments for the previous year 2017-18 are exceeding ₹ 50,000. Hence, he is a specified employee, and therefore, the motor-car facility must be taxable in his hands.

X is provided with three cars, all meant for both official and personal purpose. However, only one among them must be taxable as used for both purposes and the remaining must be taxable as used for personal purposes.

Where the choice of employee was given, it could have been taxed accordingly. In the absence of any choice of employee, the following options are available:

Option 1: To consider Car 1 as used for both purposes and other two cars as used for personal purposes.

Option 2: To consider Car 2 as used for both purposes and other two cars as used for personal purposes.

Option 3: To consider Car 3 as used for both purposes and other two cars as used for personal purposes.

The following table summarises the taxable value under all the above options:

	Option 1 (Car 1 is treated as used for both purposes) ₹	Option 2 (Car 2 is treated as used for both purposes) ₹	Option 3 (Car 3 is treated as used for both purposes) ₹
Value of Car 1	39,600	1,28,300	1,28,300
Value of Car 2	1,25,700	21,600	1,25,700
Value of Car 3	87,600	87,600	21,600
Total	2,52,900	2,37,400	2,75,500

Since, the total taxable value is lowest under option 2, it is advisable for Mr. X to **assess Car 2 as used for both ‘official and personal purposes’** and Cars 1 and 3 as used for private purposes.

Working Note:

	Car 1	Car 2	Car 3
Value of the car if it is considered as used for both purposes (Standard Value is the taxable value)	(₹ 2400 + ₹ 900) × 12 = ₹ 39,600	(₹ 1800 × 12) = ₹ 21,600	(₹ 1800 × 12) = ₹ 21,600
Value of the car if it is considered as used for personal purpose			
Value of Car (10% of ‘Cost of car’)	48,900	51,000	35,000
Add: Expenses met by employer	79,300	74,700	52,600
	1,28,200	1,25,700	87,600

Any Other Conveyance Facility (Other than Motor Car)

Where employee owns any other conveyance facility, other than motor car (like two wheeler, etc.), and expenses for the use of the vehicle is met or reimbursed by employer, it becomes a perquisite. The tax provisions for this benefit, in accordance with Income Tax Rule 3(2),a are summarised in the table below:

Situation	Usage of Vehicle	Taxable Under Section	Taxable Value
Vehicle is owned by employee and expenses are met by employer	Used for only personal purposes	17(2)(iv)	Running and maintenance expenses met or reimbursed by employer.
Vehicle is owned by employee and expenses are met by employer	Used for both official and personal purposes	17(2)(iv)	Running and maintenance expenses met or reimbursed by employer <i>minus</i> ₹900 per month, or any higher amount if log book for use of vehicle is maintained.
Vehicle is owned by employee and expenses are met by employee	Any purpose	Not a perquisite	

Case where other conveyance facility is not taxable is given under 'tax-free perquisites' (Item No. 9)

Domestic Servant Facility

Where employee is provided facility of domestic servants (maid-servant, sweeper, gardener, cook, watchman, etc.), it is a benefit which is taxable as perquisite as per provisions under Income Tax Rule 3(3).

The employer can provide servant facility to employee in two ways, viz.,

1. Employer appoints servants at employees' residence and pays their salary.
2. Employee appoints servants at his residence, their salary being paid by employer.

Where employer appoints servants at employees' residence and pays their salary, the facility is taxable **under section 17(2)(iii)**, that is, only if employee is a 'specified employee'.

Where employee appoints servants at his residence, and their salaries are paid by employer, the facility is taxable **under section 17(2)(iv)** as 'personal obligation of employer met or reimbursed by employer'.

In either case, the taxable value is—

Cost to employer (i.e., salary paid by employer to domestic servants of employee)	XXX
Less: any amount, recovered from employee	XXX
	XXX

Notes:

1. Usually, employer appoints servants at employee's residence, when employee is residing in an accommodation which is owned by employer.
2. Where employee is residing in accommodation owned by employer and a gardener is appointed by employer for such accommodation, then 'salary paid to gardener' by employer and 'garden maintenance expenses' must not be separately considered. That is, these items must not be taxable in the specified situation.

Illustration 56 Problem on tax-treatment of domestic servant facility

Mr. X and Mr. Y are working for M/s Gama Ltd. As per salary fixation norms, the following perquisites were offered:

- (i) For Mr. X, who engaged a domestic servant for ₹500 per month, his employer reimbursed the entire salary paid to the domestic servant.
- (ii) For Mr. Y, he was provided with a domestic servant @ ₹500 per month as part of remuneration package.

You are required to comment on the taxability of the above in the hands of Mr. X and Mr. Y who are not specified employees.

Solution:**Case (i):**

In this case, the servant is appointed by X, the employee and the salary is reimbursed by employer. Hence, it is a perquisite taxable in the hands of all employees, **under section 17(2)(iv)**, as 'personal obligation of employee met or reimbursed by employer'.

Taxable Value = $(₹500 \times 12) = ₹6,000$.

Case (ii):

In this case, the servant is appointed by employer of Y, for Y's domestic help. Hence, the facility is taxable under section 17(2)(iii), only if employee is a 'specified employee'.

The problem clearly states that Y is not a specified employee. Hence, the domestic servant facility is not taxable in the hands of Mr. Y.

Facility of Gas, Electricity and Water Supply

Employer may provide the facility of free or concessional supply of gas, electricity and water in the following two ways:

1. Employer may supply the above facilities from his internal sources.
2. Employee may obtain these facilities from external sources, the bills for which are paid or reimbursed by employer.

The tax provisions for this facility, in accordance with Income Tax Rule 3(4), are summarised in the following table—

Situation	Taxable under section	Taxable Value
The Gas, Electricity or Water connections are in the name of employer , and these facilities are supplied from internal sources of employer to employee's residence	17(2)(iii)	Cost to employer <i>minus</i> any amount recovered from employee
The Gas, Electricity or Water connections are in the name of employer – the facilities are obtained from external agencies , bills for which are paid by employer .	17(2)(iii)	Bill amount paid or reimbursed by employer
The Gas, Electricity or Water connections are not in the name of employer , and these facilities are supplied from internal sources of employer to employee's residence	17(2)(iv)	Cost to employer <i>minus</i> any amount recovered from employee
The Gas, Electricity or Water connections are not in the name of employer – the facilities are obtained from external agencies , bills for which are paid by employer .	17(2)(iv)	Bill amount paid or reimbursed by employer

Notes:

1. Usually, the Electricity and Water connections will be in the name of the Owner of the House Property. So, where the accommodation in which employee is residing, is owned by employer, the connections are said to be in the name of employer.
2. Gas connection will be in the name of Subscriber. Where the Gas was subscribed for by the employer, the connection is said to be in the name of employer.

Education Facility to 'members of the household' of the employee

Employer can provide education facility to 'members of the household' of employee in the following two ways:

1. Members of the household of the employee are offered free or concessional education in an educational institution run by employer.
2. Members of the household of the employee are getting educated in an institution which does not belong to employer, but the expense for education are met or reimbursed by employer.

The tax provisions with regard to this facility, in accordance with Income Tax Rule 3(5), are summarised in the following table:

Situation	Taxable under Section	Taxable Value
Employee's children are getting educated in an institution owned and maintained by employer , and they are offered free or concessional education	17(2)(iii)	Cost of such education in a similar institution in or near the locality <i>minus</i> ₹1000 per month per child <i>minus</i> any amount recovered from employee

Situation	Taxable under Section	Taxable Value
Other ‘members of the household’ of employee (i.e., other than employee’s children) are getting educated in an institution owned and maintained by employer , and they are offered free or concessional education	17(2)(iii)	Cost of such education in a similar institution in or near the locality minus any amount recovered from employee
‘Members of the Household’ of the employee are getting educated in an outside institution (which is not owned and maintained by employer) – education expenses are met or reimbursed by employer – the fee receipts are in the name of employer .	17(2)(iii)	Amount of expenditure met or reimbursed by employer.
‘Members of the Household’ of the employee are getting educated in an outside institution (which is not owned and maintained by employer) – education expenses are met or reimbursed by employer – the fee receipts are not in the name of employer (It is either in the name of the student or employee or the parent)	17(2)(iv)	Amount of expenditure met or reimbursed by employer.

Cases where education facility are not taxable is given under ‘tax-free perquisites’ – (Item No. 10)

Transport facility provided by a transport undertaking to the employee or ‘members of the household’ of its employees

Where a transport undertaking provides free or concessional transport facility to its employees or ‘members of the household’ of the employees, the benefit is taxable in the hands of employees as perquisite **under section 17(2)(iii)**, only if the employee is a specified employee, in accordance with provisions under Income Tax Rule 3(6).

The taxable value of this benefit is–

Taxable Value = value at which such benefit is offered by the employer to the public **minus** any amount recovered from employee.

Case where transport facility provided by a transport undertaking is not taxable is given under ‘tax-free perquisites’ – (Item No. 11)

Any other Benefit or Facility

Any other benefit extended by employer to employee of 'members of the household' of the employee, other than those listed under 'tax-free perquisites' and those which are specifically taxable, is taxable in the hands of employee under section 17(2)(iii), only if the employee is a 'specified employee', in accordance with provisions under Income Tax Rule 3(10).

The Taxable value of any such other benefit or facility will be the **cost to employer minus** any amount recovered from employee.

Illustration 57 Problem on tax-treatment of various perquisites

X, employed in ABC Co. Ltd., as finance manager, gives the list of perquisites provided by the company to him for the entire financial year 2017-18:

- (i) Medical facility given to his family in a hospital maintained by the company. The estimated value of benefit because of such facility is ₹40,000.
- (ii) Domestic servant was provided at the residence of X. Salary of domestic servant is ₹1,500 per month. The servant was engaged by him and the salary is reimbursed by the company (employer). In case, the company has employed the domestic servant, what is the value of perquisite?
- (iii) Free education was provided to his two children A and B in a school maintained and owned by the company. The cost of such education for A is computed at ₹900 per month and for B at ₹1200 per month. No amount was recovered by the company for such education facility from X.
- (iv) The employer has provided movable assets such as television, refrigerator and air-conditioner at the residence of X. The actual cost of such assets provided to the employee is ₹1,10,000.
- (v) A gift voucher worth ₹10,000 was given on the occasion of his marriage anniversary. It is given by the company to all employees above certain grade.

State the taxability or otherwise of the above said perquisites and compute the total value of taxable perquisites.

Solution:**Case (i):**

Medical facility given to employee and his family members, at a hospital owned and maintained by employer is **tax-free**. Hence, the taxable value is **Nil**.

Case (ii):

Taxable value of domestic servant facility = $(₹1,500 \times 12) = ₹18,000$.

Where the *servant is appointed by employee* and salary is paid by employer, the facility is taxable in the hands of all employees under section 17(2)(iv); and where the *servant was provided by employer*, then the facility is taxable only in the hands of 'specified employees', under section 17(2)(iii). In either case, the taxable value remains same.

Case (iii):

The education facility is taxable only if the employee is a specified employee, under section 17(2)(iii).

The taxable value is calculated as follows:

	₹
Child A: [₹ 900 per month (–) ₹ 1000 per month] × 12 Months	Nil
Child B: [₹ 1,200 per month (–) ₹ 1000 per month] × 12 Months	2,400

When employee's children are getting educated in an institution owned and maintained by employer, the cost of education is tax-free up to ₹ 1,000 per month, per child. Since, the cost of A's education is ₹ 900 per month, it is completely tax-free.

So, the taxable value of education facility is ₹ 2,400.

Case (iv):

Movable assets of employer given for employee's use is taxable as 'fringe benefits' under section 17(2)(viii).

$$\text{Taxable value} = (\text{₹ } 1,10,000 \times 10/100) = \text{₹ } 11,000.$$

Case (v):

Gifts given to employee is taxable as 'fringe benefit' under section 17(2)(viii).

Gifts in cash is fully taxable and 'aggregate value' of gifts in kind is tax-free up to ₹ 5,000.

So, Taxable Value of Gift is – [₹ 10,000 (–) ₹ 5,000] = ₹ 5,000.

Total value of taxable perquisites

Perquisite	X is not a specified employee ₹	X is a specified employee ₹
Medical Facility	Nil	Nil
Domestic Servant	18,000	18,000
Children Education Facility	Nil	2,400
Use of Employer's movable assets	11,000	11,000
Gifts	5,000	5,000
	34,000	36,400

PROFITS IN LIEU OF OR IN ADDITION TO SALARY UNDER SECTION 17(3)**9.11**

All monetary payments provided by employer, other than those which are included under Forms of Salary and Allowances, are considered under this head. Any other monetary benefit received by employee, from his employer, may be in addition to his salary or in lieu of his salary.

The following are the examples of benefits that must be considered under this head, along with its tax treatment.

Sl No.	Income or Benefit	Tax Treatment
1.	Payment in appreciation of services, like awards and rewards	Fully Taxable
2.	Compensation for modification in terms and conditions of employment	Fully Taxable
3.	Employer's contribution and interest thereon included in 'accumulated balance' of Un-recognised Provident Fund. (Refer to discussion under 'Provident Fund')	Fully Taxable
4.	Payment received on maturity of Keyman Insurance Policy (including bonus), when assigned by employer	Fully Taxable
5.	Any amount due or received before joining or after cessation of employment	Fully Taxable
6.	Voluntary Retirement Compensation	See explanation below
7.	Retrenchment Compensation	See explanation below
8.	Any other sum received from employer	Fully Taxable

Voluntary Retirement Compensation

When an employee opts of voluntary retirement, the compensation he is given is called 'voluntary Retirement Compensation'.

The tax provisions relating to 'voluntary compensation' received by employee, are as follows—

- Voluntary retirement compensation is **exempt up to ₹5,00,000 [under section 10(10C)]**, when the *employee of entities mentioned in point 3 below*, had opted for voluntary retirement under a *scheme offered by the employer* as per *guidelines prescribed* (listed in Point 4 below) under Income Tax Rule 2(BA).
- In any other case, the voluntary retirement compensation received by an employee, is **fully taxable**.
- Entities, employees of which are eligible for exemption under section 10(10C)***
 - a public sector company,
 - any other company,
 - an authority established under a Central, State or Provincial Act,
 - a local authority,
 - a co-operative society,
 - a University established or incorporated by or under a Central, State or Provincial Act and an institution declared to by a University under section 3 of the University Grants Commission, 1956,
 - an Indian Institute of Technology within the meaning of clause (g) of Section 3 of the Institutes of Technology Act, 1961,
 - such institute of management as the Central Government may, by notification in the Official Gazette, specify in this behalf.
 - State Government,

- (j) Central Government,
- (k) institutions having importance throughout India or in any State or States as may be notified.

4. *Prescribed Guidelines*

- (i) The voluntary retirement scheme applies to an employee, who has completed 10 years of service or completed 40 years of age;
- (ii) The scheme should apply to all employees (by whatever name called) including workers and executives of a company or of an authority or of a co-operative society, as the case may be, excepting Directors of a company or of a co-operative society;
- (iii) The scheme of voluntary retirement or voluntary separation should have been drawn to result in overall reduction in the existing strength of the employees;
- (iv) The vacancy caused by the voluntary retirement or voluntary separation is not to be filled up;
- (v) The retiring employee of a company shall not be employed in another company or concern belonging to the same management;
- (vi) The amount receivable on account of voluntary retirement or voluntary separation of the employee does not exceed—
 - (a) The amount equivalent to 3 months salary for each completed year of service, or
 - (b) Salary at the time of retirement multiplied by the balance months of service left before the date of his retirement on superannuation.

Retrenchment Compensation

‘Retrenchment Compensation’ includes any compensation received by an employee at the time of retrenchment under—

- (a) The Industrial Disputes Act, 1947; or
- (b) Any other Act or Rules or any order or notification issued there under; or
- (c) Any standing order; or
- (d) Any award, contract of service or otherwise.

Following is the format for computing the taxable amount of Retrenchment Compensation received by an employee:

	₹	₹
Amount of Retrenchment Compensation Received		XXX
Less: <i>Exempt under section 10(10B), being least of the following:</i>		
(a) Compensation according to provisions of section 25(FB) of the Industrial Disputes Act, 1947	XXX	
(b) Maximum Limit	5,00,000	
(c) Amount of Retrenchment Compensation Received	XXX	XXX
Taxable Retrenchment Compensation		XXX

Notes:

According to Industrial Disputes Act, 1947 the compensation must be 15 days 'average salary' for each completed year of service or part thereof in excess of 6 months.

'Average Salary' refers to **total** of taxable monetary payments of last 3 months of service (excluding bonus, commission and gratuity), **divided by 3**.

Illustration 58 Problem on computation of Taxable Retrenchment Compensation

Mr. Gobind received retrenchment compensation of ₹ 10,00,000 after 30 years 4 months of service. At the time of retrenchment, he was receiving basic salary of ₹ 20,000 per month, dearness allowance of ₹ 5,000 per month. Compute his taxable retrenchment compensation.

Solution:

1. Number of years of service (rounded off) – 30
2. 'Average Salary' – **₹ 25,000 per month** (assuming same amount of Basic Salary and Dearness Allowance for last 3 months of service)
3. ***Taxable Retrenchment Compensation:***

	₹	₹
Amount of Retrenchment Compensation Received		10,00,000
Less: <i>Exempt under section 10(10B), being least of the following:</i>		
(a) Compensation according to provisions of section 25(FB) of the Industrial Disputes Act, 1947 [15/30 × ₹ 25,000 × 30 Years]	3,75,000	
(b) Maximum Limit	5,00,000	
(c) Amount of Retrenchment Compensation Received	10,00,000	3,75,000
Taxable Retrenchment Compensation		6,25,000

PROBLEMS ON COMPUTATION OF TAXABLE INCOME FROM SALARY

While computing taxable salary, it is advisable to consider the items in the following order:

1. Basic Salary
2. Dearness Pay
3. Dearness Allowance
4. Other Forms of Salary
5. All other Allowances
6. Employers' Contribution to Provident Fund
7. Interest on accumulated balance of Provident Fund
8. Tax-free Perquisites
9. Perquisites taxable in the hands of all employees
10. Other perquisites (which are taxable only in the hands of 'specified employees')
11. Any other monetary payments (that is, 'Profits in Lieu of or in Addition to Salary')

Illustration 59 Problem on Computation of Taxable Salary

Mr. Balaji, employed as production manager in Beta Ltd., furnishes you the following information for the year ended 31-03-2018:

- (i) Basic salary up to 31-10-2017 ₹ 50,000 per month
 Basic salary from 01-11-2017 ₹ 60,000 per month

Note: Salary is due and paid on the last day of every month.

- (ii) Dearness Allowance @ 40% of basic salary.
 (iii) Bonus equal to one month's salary. Paid in October 2017 on basic salary plus dearness allowance applicable for that month.
 (iv) Contribution of employer to recognised provident fund account of the employee @ 16% of basic salary.
 (v) Profession tax paid ₹ 3,000 of which ₹ 2,000 was paid by employer.
 (vi) Facility of laptop and computer was provided to Balaji for both official and personal use. Cost of laptop ₹ 45,000 and computer ₹ 35,000 were acquired by the company on 01-12-2017.
 (vii) Motor car owned by the employer (cubic capacity of engine exceeds 1.6 litres) provided to the employee from 01.11.2017 meant for both official and personal use. Repair and running expenses of ₹ 45,000 from 01-11-2017 to 31-03-2018, were fully met by the employer. The motor car was self-driven by the employee.
 (viii) Leave travel concession given to employee, his wife and three children (one daughter aged 7 and twin sons aged 3). Cost of air tickets (economy class) reimbursed by the employer ₹ 30,000 for adults and ₹ 45,000 for three children. Balaji is eligible for availing exemption this year to the extent it is permissible in law.

Compute the salary income chargeable to tax in the hands of Mr. Balaji for the assessment year 2018-19.

Solution:**Computation of Taxable Salary**

Assessee:	Mr. Balaji	Assessment Year:	2018-19
Status:	Resident and Ordinarily a Resident	Previous Year:	2017-18
Category:	Non-Government Employee		

	₹	₹
Basic Salary [(₹ 50,000 × 7) + (₹ 60,000 × 5)]		6,50,000
Dearness Allowance [40% of ₹ 6,50,000]		2,60,000
Bonus [₹ 50,000 + 40% of ₹ 50,000]		70,000
Employer's Contribution to Recognised Provident Fund (See Note No. 1)		26,000

	₹	₹
Facility of Laptop and Computer provided by Employer	Tax-Free	Nil
Leave Travel Concession (See Note No. 2)	Tax-Free	Nil
Professional Tax of employee paid by employer		2,000
Motor-car Facility (See Note No. 3) – (₹2,400 × 5)		12,000
Gross Salary		10,20,000
Less: Deductions under Section 16		
(ii) Entertainment Allowance	Nil	
(iii) Professional Tax Paid	3,000	3,000
Taxable Salary		10,17,000

Notes:

- Employer's Contribution to Employee's Provident Fund is taxable to the extent the contribution exceeds 12% of "Salary".

For this purpose, "Salary" is:

	₹
Basic Salary	6,50,000
Dearness Allowance (not entering into retirement benefits)	Nil
	6,50,000
Employer's Contribution (16% of Basic salary – 16% of ₹6,50,000)	1,04,000
Less: 12% of "Salary" – 12% of ₹6,50,000	78,000
Excess	26,000

- Leave Travel Concession is exempt under section 10(5), to the extent of least of the following:

- Amount of expenditure incurred of travel and employee and family members.
- Amount as per guidelines, and
- Amount of leave travel concession received.

It is assumed that the cost of air tickets reimbursed (₹75,000), represents the actual travel expenditure and the amount as per guideline. Hence, all the limits being same, the entire amount of leave travel concession has been taken as exempt.

'Family' includes only two children born on or after 1st October 1998. However, after one child, if multiple children are born, it is considered as 'one child'. Employee has one child aged 7 years and twin children aged 3, it is evident that first child was a single child and in the second birth, twins were born. For tax purposes, it will be considered as two children only and hence all children, in this case, become part of 'family members'.

3. Employer has provided a big car to employee and has met the running and maintenance expenses. The car has been used for both official and personal purposes. Hence, standard value must be taken as taxable value. The standard value is ₹2,400 per month. No driver facility is provided to employee.

Accordingly, the taxable value for 5 months from November 2017 to March 2018 is—
 $(₹2,400 \times 5) = ₹12,000$.

This facility is taxable only if Mr. Balaji is a 'specified employee'. A cursory glance at his taxable monetary emoluments (in this case, Basic Salary, Dearness Allowance and Bonus) indicates that the taxable amount of monetary receipts, after providing for deductions under section 16, exceeds ₹50,000. Hence, Balaji is a specified employee. Therefore, the value of motor-car facility is taxable in his hands.

4. Professional Tax of employee paid by employer is a perquisite taxable under section 17(2) (iv) as 'personal obligation of employee met by employer'. Hence, the amount of ₹2,000 has been included in taxable salary.

Professional tax of employee paid is deductible under section 16(iii), irrespective of who makes the payment. Hence, the amount of ₹3,000 (which is the amount of Professional Tax paid) is completely deducted.

Illustration 60 Problem on Computation of Taxable Salary

From the following details, find out the salary chargeable to tax of Mr. Anand for the assessment year 2018-19:

Mr. Anand is a regular employee of Malpani Ltd. In Mumbai. He was appointed on 01.03.2017 in the scale of ₹25,000–2500–35000. He is paid dearness allowance (which forms part of salary for retirement benefits) @ 15% of basic pay and bonus equivalent to one and half month's basic pay at the end of the year. He contributes 18% of his salary (basic pay plus dearness allowance) towards recognised provident fund and the company contributes the same amount.

He is provided free housing facility which has been taken on rent by the company at ₹15,000 per month. He is also provided with following facilities:

- (a) The company reimbursed the medical treatment bill of ₹40,000 of his daughter, who is dependent on him.
- (b) The monthly salary of ₹2,000 of a house keeper is reimbursed by the company.
- (c) He is getting telephone allowance @ ₹1000 per month.
- (d) A gift voucher of ₹4,700 was given on the occasion of his marriage anniversary.
- (e) The company pays medical insurance premium to effect an insurance on the health of Mr. Anand ₹12,000.
- (f) Motor car running and maintenance charges fully paid by the employer of ₹36,600 (the motor car is owned and driven by Mr. Anand. The engine capacity is below 1.6 litres. The motor car is used for both official and personal purposes by the employee).
- (g) Value of free lunch provided during office hours is ₹2,200.

Solution:**Computation of Taxable Salary****Assessee:** Mr. Anand**Assessment Year:** 2018-19**Status:** Resident and Ordinarily a Resident**Previous Year:** 2017-18**Category:** Non-Government Employee

	₹	₹
Basic Salary (See Note No. 1)		3,02,500.00
Bonus (See Note No. 2)		41,250.00
Dearness Allowance (15% of Basic Pay)		45,375.00
Telephone Allowance (Fully Taxable) – ₹1,000 × 12		12,000.00
Employer's Contribution to Recognised Provident Fund (See Note No. 3)		20,872.50
Medical Insurance Premium on Anand's policy paid by employer	Tax-Free	Nil
Medical treatment expenses of Anand's daughter, reimbursed by employer (₹40,000 – ₹15,000) – See Note No. 4		25,000
Gift Voucher (Completely tax-free since the gift is less than ₹5,000)	Tax-Free	Nil
Rent-free Accommodation (See Note No. 5)		60,168.75
Motor Car Facility (See Note No. 6)		7,800.00
Free lunch provided during office hours (assuming cost per meal is less than ₹50, it is fully tax-free)	Tax-Free	Nil
House Keeper's Salary reimbursed by employer (₹2,000 × 12)		24,000.00
Gross Salary		5,38,966.25
Less: Deductions under section 16		Nil
Taxable Salary		5,38,966.25

Notes:**1. 'Basic Salary'**

Employee is appointed in the month of March 2017 in the pay-scale of ₹25,000 – ₹2,500 – ₹35,000 per month. His Basic Salary will be as follows–

	₹ Per month
From March 2017 to February 2018	25,000
From March 2018 to February 2019	27,500
and so on.	

Assuming Salary falls due in the same month of service, for previous year 2017-18, the Basic Salary is–

$$(\text{₹}25,000 \times 11) + (\text{₹}27,500 \times 1) = \text{₹}3,02,500.$$

2. Bonus:

Bonus is paid at the end of the year and it is equivalent to one and a half month's basic pay. For the month of March 2018 (being the last month of the year), the Basic Pay was ₹27,500. So, Bonus for the year 2017-18 is–

$$\text{₹}27,500 \times 1.5 = \text{₹}41,250.$$

3. Employer's Contribution to Recognised Provident Fund:

Employer's Contribution to Recognised Provident Fund of Employee is taxable if the contribution exceeds 12% of "Salary"

A. "Salary" for this purpose:

	₹
Basic Salary	3,02,500
Dearness Allowance (since it enters into retirement benefits)	45,375
	<u>3,47,875</u>

B. Calculation of 'Taxable Contribution':

	₹
Employer's Contribution [18% of (₹3,02,500 + ₹45,375)]	62,617.50
Less: 12% of "Salary" (12% of ₹3,47,875)	41,745.00
Excess	<u>20,872.50</u>

4. Medical Benefits

- A. Medical insurance premium on policy of employee and his family members, paid or reimbursed by employer is tax-free.
- B. Medical treatment expenses of employee's daughter, reimbursed by employer is tax-free. However, since the details of treatment is not known, it is assumed that the treatment is in private hospital and hence the benefit has been considered tax-free up to ₹15,000.

5. Valuation of Rent-free Accommodation:

A. "Salary" for this purpose:

	₹
Basic Salary	3,02,500
Telephone Allowance	12,000
Bonus	41,250
Dearness Allowance (considered since it enters into retirement benefits)	45,375
	<u>4,01,125</u>

B. Valuation of Rent-free Unfurnished House Accommodation:

The Accommodation provided to employee is hired by employer. Hence, the value of rent-free unfurnished accommodation is—

Actual Rent payable by employer (₹15,000 × 12) ₹1,80,000

Or

15% of "Salary" for this purpose (15% of ₹4,01,125) ₹60,168.75

Whichever is less.

So, the value of Rent-free Accommodation is **₹60,168.75**

6. Valuation of Motor-Car Facility:

Motor car is owned by employee, used by him for both official and personal purposes and the expenses are met by employer. The facility is taxable under section 17(2)(iv).

The taxable value of the perquisite is—

Amount of expenditure met by employer *minus* standard valuation.

When the car is a small car and expenses are met by employer, the standard value is ₹2,400 per month.

So, the taxable value of the car facility is—

₹36,600 (–) [₹2,400 × 12] = **₹7,800.**

7. It is assumed that the house-keeper is appointed by employee. Accordingly, it is taxable under Section 17(2)(iv).

8. None of the perquisites given to employee are taxable under Section 17(2)(iii). Hence, there was no need to ascertain whether Anand is a 'specified employee'.

Illustration 61 Problem on Computation of Taxable Salary

Mr. X retired from the services of M/s Y Ltd. on 31.01.2018 after completing service of 30 years and one month. He had joined the company in December 1987 at the age of 30 years and received the following on his retirement:

- (i) Gratuity ₹6,00,000. He was covered under the Payment of Gratuity Act, 1972.
- (ii) Leave encashment of ₹3,30,000 for 330 days leave balance in his account. He was credited 30 days leave for each completed year of service.
- (iii) As per the scheme of the company, he was offered a car which was purchased on 01-02-2014 by the company for ₹5,00,000. Company has recovered ₹2,00,000 from him for the car. Company depreciates the vehicles at the rate of 15% on Straight Line Method.
- (iv) An amount of ₹3,90,000 as commutation of pension for 2/3rd of his pension commutation.
- (v) Company presented him a gift voucher worth ₹6,000 on his retirement.
- (vi) His colleagues also gifted him a Television (LCD) worth ₹50,000 from their own contribution.

Following are the other particulars:

- (a) He has drawn a basic salary of ₹20,000 and 50% dearness allowance per month for the period from 01-04-2017 to 31-01-2018.
- (b) Received pension of ₹5,000 per month for the period 01-02-2018 to 31-03-2018 after commutation of pension.

Compute his Taxable Salary from the above for the assessment year 2018-19.

Solution:**Computation of Taxable Salary**

Assessee:	Mr. X	Assessment Year:	2018-19
Status:	Resident and Ordinarily a Resident	Previous Year:	2017-18
Category:	Non-Government Employee		

	₹	₹
Basic Salary ($\text{₹}20,000 \times 10$)		2,00,000
Dearness Allowance (50% of ₹2,00,000)		1,00,000
Taxable Gratuity (See Note No. 1)		80,769
Taxable Leave Salary (See Note No. 2)		1,30,000
Taxable Pension (See Note No. 3)		2,05,000
Gift Voucher from employer ($\text{₹}6,000 - \text{₹}5,000$)		1,000
Transfer of Motor Car by the company (See Note No. 4)		56,000
Gross Salary		7,72,769
Less: Deductions under section 16		Nil
Taxable Salary		7,72,769

Notes:**1. Computation of 'Taxable Gratuity':**

	₹	₹
Actual Gratuity Received		6,00,000
Less: <i>Exempt under section 10(10)(ii), being least of the following:</i>		
(a) $15/26 \times \text{'Last drawn Salary'} \times \text{Number of years of service. [} 15/26 \times \text{₹}30,000 \times 30 \text{]}$	5,19,231	
(b) Maximum Limit	10,00,000	
(c) Actual Gratuity Received	6,00,000	5,19,231
Taxable Gratuity		80,769

Notes:

- (i) Number of years of service = 30 (rounded off).
- (ii) **'Last Drawn Salary'** (Calculated on the basis of salary for last month of service, i.e., December 2017)

Basic Salary	₹ 20,000
Dearness Allowance (50% of ₹20,000)	₹ 10,000
	<u>₹ 30,000</u>

Note: There is no condition to be fulfilled for considering Dearness Allowance, when the employee is covered under 'Payment of Gratuity Act'.

2. Computation of 'Taxable Leave Salary':

	₹	₹
Actual Leave Salary Received		3,30,000
Less: <i>Exempt under section 10(10AA)(ii), being least of the following:</i>		
(a) Leave at the credit of employee × "Average Salary" [11 × ₹20,000]	2,20,000	
(b) 10 Months' "Average Salary" [10 × ₹20,000]	2,00,000	
(c) Maximum Limit	3,00,000	
(d) Actual Leave Salary Received	3,30,000	2,00,000
Taxable Leave Salary		1,30,000

Notes:

- (i) Leave at the credit of employee given in the problem is calculated on the basis of employer's leave entitlement. This must not be considered for tax purposes.
- (ii) For tax purposes, the leave at the credit of employee must be calculated as follows:

Number of completed years of service – 30

Leave entitlement – 30 days (entitled by employer) **or** 30 days (limit as per Income Tax Provisions), whichever is less, for each completed year of service. So, 'Leave Entitlement' is 900 days (i.e., 30 days × 30 years).

Leave availed by employee during service period.

Leave credited by employer each year – 30 days. So, for 30 years it is 900 days. Leave at the credit of employee at the time of retirement is 330 days. So, leave availed by employee during service period is 900 – 330 days = 570 days.

Leave at the credit of employee = 900 days – 570 days = **330 days or 11 Months** (i.e., 330 days/30 days).

- (iii) **"Average Salary"** (Calculated on the basis of Salary for ten months preceding the date of retirement, i.e., April 2017 to January 2018)

	₹
Basic Salary (₹20,000 × 10)	2,00,000
Dearness Allowance (Not considered, since there is no mention or hint about DA entering into retirement benefits)	Nil
	<u>2,00,000</u>

'Average Salary' = ₹2,00,000/10 = **₹20,000.**

3. Computation of 'Taxable Pension'

During this previous year, assessee has commuted pension. Hence, for calculating taxable pension the following must be ascertained:

- (i) Un-commuted Pension (Normal Pension) – ₹5000 per month from February 2018.
So, for two months – ₹5,000 × 2 = ₹10,000.
- (ii) Commuted Portion of Pension – 2/3.
- (iii) Commuted Value of Pension (lump-sum received) – ₹3,90,000.
- (iv) Actual Value of Commuted Pension – $3,90,000 \times \frac{3}{2} = ₹5,85,000$.

	₹	₹
Normal or Un-commuted Pension		10,000
Commuted Value of Pension	3,90,000	
Less: Exempt under section 10(10A)(ii)–		
One-third of 'Actual Value of Commuted Pension		
($1/3 \times ₹5,85,000$) – since Gratuity is received.	1,95,000	1,95,000
Taxable Pension		2,05,000

4. Valuation of Motor Car transferred to employee:

Particulars	Motor-Car
Period for which motor-car was used by employer (i.e., duration between date of acquisition by employer and date of transfer to employee – From 01.02.2014 to 31.01.2018)	3 Years and 11 Months
No. of Completed Years	3
Rate of Normal Wear and Tear Note: The rate of depreciation used by the company is irrelevant. The normal wear and tear must be considered as specified under Income Tax Rule 3(7)	20% of 'reduced balance'
Value of the asset at the time of its transfer to employee	₹
Original Cost:	5,00,000
Less: Normal wear and tear for first completed year	1,00,000
	4,00,000
Less: Normal wear and tear for second completed year	80,000
	3,20,000
Less: Normal wear and tear for third completed year	64,000
	2,56,000
Less: Consideration payable by employee	2,00,000
	56,000

5. Television gifted by colleagues is neither 'income from salary', nor an income which can be considered under any other head of income.

Illustration 62 Problem on Computation of Taxable Salary

Mr. Shivakumar gives the following particulars of income for the year ending 31-03-2018: Basic Salary (after deduction of tax at source and own contribution to Recognised Provident Fund at

15%) ₹4,75,000; Dearness Allowance 52%; HRA 30%; City Compensatory Allowance ₹300 per month; Tax deducted at source ₹47,750; Employer's contribution to Recognised Provident Fund ₹97,550; Interest credited on June 22, 2017 to Recognised Provident Fund at 12.5% ₹56,250; Holiday home facility worth ₹45,200. During the year he has paid ₹2,400 as professional tax. Determine the Taxable Salary Income of Mr. Shivakumar for the Assessment Year 2018-19.

Solution:**Computation of Taxable Salary**

Assessee: Mr. Shivakumar **Assessment Year:** 2018-19
Status: Resident and Ordinarily a Resident **Previous Year:** 2017-18
Category: Non-Government Employee

	₹	₹
Basic Salary (See Note 1)		6,15,000
Dearness Allowance (₹6,15,000 × 52%)		3,19,800
House Rent Allowance (₹6,15,000 × 30%)		1,84,500
City Compensatory Allowance (₹300 × 12)		3,600
Employer's contribution to RPF over and above 12% of salary (See Note 2)		23,950
Interest credited to RPF over and above 9.5% (See Note 3)		13,500
Holiday home facility		45,200
<u>Gross Salary</u>		12,05,550
Less: Deductions u/s 16		
(ii) Entertainment Allowance	Nil	
(iii) Professional Tax paid	2,400	2,400
Taxable Salary		12,03,150

Notes:

- Basic salary **after** tax deduction at source and own contribution to RPF is given. Since deduction towards RPF is 15%, the 'net amount received' plus 'tax deducted at source' represents 85%. Thus ₹5,22,750 (i.e., ₹4,75,000 + ₹47,750) represents 85%. Therefore, basic salary **before** deduction of income tax and own contribution to RPF is ₹6,15,000 (i.e., $5,22,750 \times 100/85$).
- Actual contribution to Recognised Provident Fund by the employer is ₹97,550. 12% of salary is ₹73,800 (i.e., $6,15,000 \times 12\%$). Therefore, the excess contribution is ₹23,950 ($97,750 - 73,800$). Since, the problem is silent regarding Dearness Allowance, it is assumed that Dearness Allowance does not enter into retirement benefits.
- Interest credited to RPF over and above 9.5% per annum is taxable. Since the interest credited is at 12.5%, the excess interest of 3% (i.e., $12.5\% - 9.5\%$) is taken as taxable. It is calculated as follows:
 If 12.5% represents ₹56,250 how much is 3% i.e.,

$$12.5\% = 56,250$$

$$3\% = ?$$

Therefore, excess interest credited is $(56,250/12.5) \times 3 = ₹13,500$.

Illustration 63 Problem on Computation of Taxable Salary

Ms. Queen is the Manager of a cloth mill. She receives every month ₹19,000 as Basic Pay, ₹4,000 as Dearness Pay, and ₹500 as Entertainment Allowance.

She owns a house but the company has provided her with the following amenities: Free services of Gardener, Sweeper and Cook each of whom is paid ₹700 p.m; free use of company's refrigerator costing ₹10,000; free supply of Gas, Water and Electricity to which the company pays ₹13,500 annually.

She herself owns a car and uses it for both official and personal purposes but the company meets all the expenses of maintaining the car. The expenses incurred by the company towards the car used for personal purposes are estimated at ₹8,450 (the company has maintained log book).

Her son is studying in a school run by the company where the cost of education is ₹18,000 p.a. but the company is collecting only ₹300 p.m. from her towards this facility.

During the year she proceeded on leave to Shimla and stayed in a holiday home maintained by the company (the company incurs an expenditure of ₹30,000 for this facility).

During the year she has paid ₹2,400 as professional tax.

Determine the Taxable Salary Income of Ms. Queen, for Assessment Year 2018-19.

Solution:

Computation of Taxable Salary

Assessee: Ms. Queen

Assessment Year: 2018-19

Status: Resident and Ordinarily a Resident

Previous Year: 2017-18

Category: Non-Government Employee

	₹	₹
Basic Pay ($₹19,000 \times 12$)		2,28,000
Dearness Pay ($₹4,000 \times 12$)		48,000
Entertainment Allowance ($₹500 \times 12$)		6,000
Free services of Gardener, Sweeper and Cook ($₹700 \times 12 \times 3$)		25,200
Free use of Refrigerator ($₹10,000 \times 10\%$)		1,000
Free supply of Gas, Water and Electricity		13,500
Car expenses paid towards personal use		8,450
School facility to son ($₹18,000 - ₹12,000 - ₹3,600$) – See Note 2.		2,400
Holiday home facility		30,000
	<u>Gross Salary</u>	<u>3,62,550</u>
Less: Deduction u/s 16(iii) – Professional Tax paid		2,400
	Taxable Salary	3,60,150

Notes:

1. Ms. Q is a specified employee as her monetary emoluments exceed ₹50,000. Hence, free services of domestic servants, free supply of gas, water, electricity, etc., are taxable in her case.
2. Taxable value in respect of school facility to son is calculated as follows—

	₹
Cost of similar education in a similar institution in the same locality	18,000
Less: Exemption for children's education @ ₹1000 per month per child (₹1,000 × 12)	12,000
	6,000
Less: Amount charged to employee (₹300 × 12)	3,600
	2,400

Illustration 64 Problem on Computation of Taxable Salary

Ms. Anuradha provides you the following details of income: Basic Salary ₹38,000; Dearness Allowance entering into retirement benefits ₹10,000; City Compensatory Allowance ₹2,000; Free use of Big Car with driver for both official and personal purposes; Free services of 3 domestic servants (Salary paid by company ₹2,000 per month per person); Free use of Gas, Electricity and Water (cost incurred by the company ₹28,000); Professional Tax paid by Anuradha ₹2,400. Compute the Taxable Salary Income of Anuradha, if

- (i) Anuradha is neither a director, nor a shareholder in the company;
- (ii) Anuradha is a director in the company.

Solution:**Case (i):**

Free use of car, free services of domestic servants and free use of gas, electricity, water, etc., are perquisites taxable only in the hands of specified employee. The problem states that Anuradha is neither a director nor a shareholder in the employer's company. Hence it needs to be ascertained whether her total monetary emoluments after deduction u/s 16 exceed ₹50,000 or not. If it exceeds, she becomes specified employee. In this case, his total monetary emoluments are arrived at as follows:

$$\begin{aligned}
 &\text{Basic Salary} + \text{Dearness Allowance} + \text{City Compensatory Allowance} - \text{Deduction u/s 16} \\
 &= 38,000 + 10,000 + 4,400 - 2,400 \\
 &= ₹50,000.
 \end{aligned}$$

As the total monetary emoluments does not exceed ₹50,000 (it is exactly ₹50,000) Anuradha is considered as a non-specified employee. Hence, the facility of free use of car, free services of domestic servants and free use of gas, electricity, water, etc., are not taxable in the hands of Anuradha. The taxable salary income is computed below:

Computation of Taxable Salary

Assessee:	Ms. Anuradha	Assessment Year: 2018-19
Status:	Resident and Ordinarily a Resident	Previous Year: 2017-18
Category:	Non-Government Employee	

	₹	₹
Basic Salary		38,000
Dearness Allowance		10,000
City Compensatory Allowance		4,400
Free use of Motor Car		Nil
Free services of Watchman, Sweeper & Gardner		Nil
Free use of Gas, Electricity and Water facilities		Nil
<u>Gross Salary</u>		52,400
Less: Deduction u/s 16(iii) – Professional Tax paid		2,400
Taxable Salary		50,000

Case (ii):

If Anuradha is a director in the employer company, she becomes a specified employee and hence, the free use of car, free services of domestic servants and free use of gas, electricity, water, etc., become perquisites taxable in her hands. The taxable salary income is computed below:

Computation of Taxable Salary

Assessee:	Ms. Anuradha	Assessment Year: 2018-19
Status:	Resident and Ordinarily a Resident	Previous Year: 2017-18
Category:	Non-Government Employee	

	₹	₹
Basic Salary		38,000
Dearness Allowance		10,000
City Compensatory Allowance		4,400
Free use of Motor Car – ₹3,300 × 12 (See Note below)		39,600
Free services of Watchman, Sweeper & Gardner (₹2,000 × 12 × 3)		72,000
Free use of Gas, Electricity and Water facilities		28,000
<u>Gross Salary</u>		1,92,000
Less: Deduction u/s 16(iii) – Professional tax paid		2,400
Taxable Salary		1,89,600

Note:

Anuradha is provided with the facility of free use of Big Car with driver for both official and personal purposes, and the log book is not maintained. Hence the guidance value of ₹2,400 per month for car + ₹900 per month for driver facility is considered as the value of perquisite in respect of motor car.

Illustration 65 Problem on Computation of Taxable Salary

Ms. Lavanya is the Marketing Manager in CBBJ Ltd., Bangalore. Her Basic Salary was ₹10,000 per month and Dearness Allowance ₹2,500 per month which formed part of salary for retirement benefits. In addition, she was entitled for the following: 2.5% commission on turnover achieved (Actual turnover ₹20 Lakhs); Furnished accommodation at a concessional rent of ₹500 per month at Bangalore for which the company paid ₹3,200 per month as rent and provided furniture costing ₹30,000; Facility of a watchman and a cook who are paid ₹600 per month and ₹1,000 per month respectively. The company also paid Ms. Lavanya's residential gas and electricity bills of ₹3,200 and ₹3,500 respectively for the whole year. During the Previous year 2017-18 she availed Leave Travel Concession of ₹4,500; reimbursement of ordinary medical expenses for treatment taken in a private nursing home ₹28,500 and Gift of a watch worth ₹38,300. Professional Tax paid by her was ₹2,400. Compute the Taxable Salary Income of Ms. Lavanya for the Assessment Year 2018-19.

Solution:**Computation of Taxable Salary****Assessee:** Ms. Lavanya**Assessment Year:** 2018-19**Status:** Resident and Ordinarily a Resident**Previous Year:** 2017-18**Category:** Non-Government Employee

	₹	₹
Basic Salary (₹10,000 × 12)		1,20,000
Dearness Allowance (₹2,500 × 12)		30,000
Commission (₹20,00,000 × 2.5%)		50,000
Value of rent free furnished accommodation (see Note No. 1 below)		27,000
Facility of a watchman (600 × 12) (see Note No. 2 below)		7,200
Facility of cook (1,000 × 12) (see Note No. 2 below)		12,000
Gas bills paid by the company (see Note No. 3 below)		3,200
Electricity bills paid by the company (see Note No. 3 below)		3,500
Leave Travel Concession	4,500	
Less: Exempted (see Note No. 4 below)	4,500	Nil
Reimbursement of medical expenses	28,500	
Less: Exempted (see Note No. 5 below)	15,000	13,500
Gift of a watch	38,300	
Less: Exempted (see Note No. 6 below)	5,000	33,300
Gross Salary		2,99,700
Less: Deductions u/s 16		
(ii) Entertainment Allowance	Nil	
(iii) Professional Tax paid	2,400	2,400
Taxable Salary		2,97,300

Notes:**1. Valuation of Rent-free Accommodation****A. “Salary” for this purpose:**

	₹
Basic Salary	1,20,000
Dearness Allowance (considered since it enters into retirement benefits)	30,000
Commission on Turnover	50,000
	2,00,000

B. Valuation of Rent-free Unfurnished House Accommodation:

The accommodation provided to employee is hired by employer. Hence, the value of rent-free unfurnished accommodation is—

Actual Rent payable by employer ($₹3,200 \times 12$) ₹38,400

Or

15% of “Salary” for this purpose (15% of ₹2,00,000) ₹30,000

Whichever is less.

So, the value of Rent-free unfurnished Accommodation is **₹30,000**.

C. Valuation of Rent-free Furnished House Accommodation:

	₹
Value of Rent-free Unfurnished Accommodation	30,000
Add: Value of Furniture (10% of ₹30,000)	3,000
	33,000

D. Valuation of Accommodation provided at concessional rent:

	₹
Value of accommodation provided at concessional rent	33,000
Less: Rent charged to employee ($₹500 \times 12$)	6,000
	27,000

- Facility of Watchman & Cook is taxable in case of specified employee. Ms. Lavanya is a specified employee as her annual monetary emoluments exceed ₹50,000. Hence, this facility is fully taxable.
- Payment of Gas bills & Electricity bills by the company is fully taxable as they are personal obligations of the employee met by employer.
- In the absence of detailed information about Leave Travel Concession, it is assumed that the entire amount is eligible for exemption.
- Since the reimbursement of medical expenses is in respect of treatment taken in a private nursing home, it is exempt up to ₹15,000.
- Gift in kind received by employee is exempt up to ₹5,000.

Illustration 66 Problem on Computation of Taxable Salary

Ms. Kalyani is a Government employee whose salary becomes due on the 1st of every month. During the Previous Year 2017-18 she has received the following emoluments and benefits: Basic ₹16,500 p.m. up to 31-08-17 and an increment of ₹500 p.m. from 1-09-2017; Dearness Allowance at 65% of Basic which fully enters for retirement benefits; City Compensatory Allowance ₹150 p.m; Entertainment Allowance ₹250 p.m (actual amount spent during the year ₹1,200); Transport Allowance ₹900 p.m; Uniform Allowance ₹650 p.m. (amount spent ₹450 p.m.); HRA 30% of Basic (rent paid ₹2,000 p.m.); Reimbursement of medical expenses incurred in Government Hospital ₹22,500. Ms. Kalyani has paid professional tax at ₹200 p.m. Determine the Taxable Salary Income of Ms. Kalyani for Assessment Year 2018-19.

Solution:**Computation of Taxable Salary**

Assessee:	Ms. Kalyani	Assessment Year:	2018-19
Status:	Resident and Ordinarily a Resident	Previous Year:	2017-18
Category:	Non-Government Employee		

	₹	₹
Basic [(₹16,500 × 6) + (₹17,000 × 6)] – See Note No. 1 below)		2,01,000
Dearness Allowance (₹2,01,000 × 65%)		1,30,650
City Compensatory Allowance (₹150 × 12)		1,800
Entertainment Allowance (₹250 × 12)		3,000
Transport Allowance (₹900 × 12)	10,800	
Less: Exempt u/s 10(14) – (₹800 × 12)	9,600	1,200
Uniform Allowance (₹650 × 12)	7,800	
Less: Exempt u/s 10(14) – ₹(450 × 12)	5,400	2,400
House Rent Allowance (₹2,01,000 × 30%)	60,300	
Less: Exempt u/s 10(13A) – See Note No. 2 below)	Nil	60,300
Reimbursement of medical expenses (See Note No. 3 below)		Nil
Gross Salary		4,00,350
Less: Deductions u/s 16		
(ii) Entertainment Allowance (See Note No. 4 below)	3,000	
(iii) Professional Tax paid	2,400	5,400
Taxable Salary		3,94,950

Notes:

- Salary falls due on the 1st of every month. Hence, for previous year 2017-18, the Basic Salary includes salary from March 2017 to February 2018. The Basic Salary from March 2017 to August 2017 is ₹16,500 per month and from September 2017 to February 2018 it is ₹17,000 after considering increment of ₹500 per month. That is, for 6 months during

previous year 2017-18, the basic salary is ₹16,500 per month and for the remaining six months, it is ₹17,000 per month.

2. *Exempted House Rent Allowance u/s 10(13A)*

A. *“Salary” for the purpose of House Rent Allowance*

	₹
Basic Salary	2,01,000
Dearness Allowance forming part of salary	1,30,650
	3,31,650

B. *Exempted House Rent Allowance*

Exempted HRA under section 10(13A) is least of the following:

(a) Actual amount of House Rent Allowance	60,300
(b) Excess of ‘rent paid’ over 10% of “Salary”(₹24,000 minus ₹33,165)	Nil
(c) 40% of “Salary” (since place of accommodation is not specified)	1,32,660
Exempted HRA, being least of the above	Nil

- Since the reimbursement of medical expenses is in respect of expenses incurred in Government Hospital, the entire amount is exempt.
- Deduction u/s 16 (ii) in respect of Entertainment Allowance. The amount of deduction is least of the following:
 - Maximum limit ₹5,000.
 - 20% of Basic Salary ₹40,200.
 - Actual Entertainment Allowance received ₹3,000.

Hence, Deduction u/s 16 (ii) is ₹3,000 being least of the above.

Note: The actual amount spent is not considered for allowing this deduction.

SUMMARY

- “Income from Salaries” is the first head of income among the five heads of income under Income Tax Act.
- An income is **chargeable** under the head “Income from Salaries” when two conditions are fulfilled – (a) The relationship between payer and assessee is in the nature of ‘employer’ and ‘employee’, and (b) The payment made by ‘employer’ to ‘assessee’ is ‘out of employment’.
- Under this head, Income is charged on ‘accrual’ or ‘receipt’ basis, whichever is earlier.
- For computing taxable salary, all payments and benefits given by employer to employee must be classified into four heads viz., Forms of Salary, Allowances and Provident Fund, Perquisites, and Profits in Lieu of Salary.

- Forms of Salary include Basic Salary, Advance Salary, Dearness Pay, Bonus, Fees, Commission, Interim Relief, Pension, Gratuity and Leave Salary.
- Allowances refer to a regular, fixed, monetary payment made by employer to employee for enabling employee to render his services comfortably.
- Allowances are classified into Exempted, Taxable and Partly Taxable. Section 10(14) gives the list of allowances which are exempt from tax and the extent to which they are exempt.
- Most commonly given allowances are Dearness Allowance, House Rent Allowance, Transport Allowance, Children Education Allowance, Hostel Expenditure Allowance and Medical Allowance.
- Apart from the tax treatment specified for each allowance, the treatment for any other allowance must be based on a general principle – ‘Allowance for Personal Purposes are fully taxable and Allowances for Official Purposes are exempt to the extent they have been used for the intended purpose’.
- A Provident Fund is a fund for the future benefit of employee. Any contribution made by employer to the Provident Fund in the name of employee, and Interest on Accumulated balance of Provident Fund are taxable under the head “Salaries”.
- The taxable extent depends on the type of Provident Fund to which employee is member of.
- The different types of Provident Fund are – Statutory Provident Fund, Recognised Provident Fund, Unrecognised Provident Fund, Approved Superannuation Fund and Unapproved Superannuation Fund.
- Perquisites are benefits or amenities provided by employer to employee based on the office or position of the employee. When benefits provided to employee does not fulfill at least one of the criteria for allowances (i.e., regularity, fixed and monetary), they are considered as perquisites.
- For tax purposes Perquisites are classified into three categories viz., Tax-free Perquisites, Perquisites taxable in the hands of all the assesseees, and Perquisites taxable in the hands of Specified Employees only.
- Perquisites taxable in the hands of all employees include– Rent Free Accommodation, Accommodation at Concessional Rent, Personal Obligations of employee met or reimbursed by employer, Life Insurance Premium paid by employer, Free or Concessional allotment of Shares under ESOP, Contribution to Approved Superannuation Fund and Fringe Benefits.
- An employee is considered as ‘Specified Employee’ when he is either a Director or holds a substantial interest in the company or has taxable monetary receipts exceeding ₹50,000.
- Perquisites taxable only in the hands of Specified employees are – Motor Car Facility, Any other Conveyance Facility, Domestic Servants, Free or Concessional Supply of Gas, Electricity and Water, Free or Concessional Education Facility to the members of the household of the employee, free transport facility provided by a transport undertaking and any other perquisite.
- The taxable value of all taxable perquisites is based on the principle of “extent of benefit to employee”.
- Profits in lieu or in addition to Salary includes – payment in appreciation of service, compensation for modification of employment terms, amount received on maturity of Keyman Insurance Policy, Retrenchment Compensation and Voluntary Retirement Compensation.
- The total of all taxable items under four heads is called “Gross Salary”.
- From “Gross Salary” when deductions are given under section 16 towards Entertainment Allowance and Employment Tax Paid, we can arrive at “Taxable Salary”.

THEORY QUESTIONS

Section A Type Questions

1. State the chargeability under the head 'Income from Salaries'.
2. What is the 'Basis of Charge' under the head 'Income from Salaries'?
3. List the major headings under the head 'Income from Salaries'.
4. List the items under 'Forms of Salary'.
5. State the tax treatment for (a) Basic Salary (b) Bonus (c) Commission (d) Interim relief.
6. State the classification of employees for the purpose of tax-treatment of Gratuity.
7. What is 'Average Salary' for Gratuity purposes?
8. Give the meaning of salary for the purpose of calculating exempted earned leave salary (Nov/Dec 2014).
9. What is 'Average Salary' for the purpose of Leave Salary?
10. State the classification of employees for tax-treatment of Commuted Pension.
11. What is meant by an Allowance? **(Bangalore University, B.Com., Nov/Dec 2014 & 2017)**
12. What are Allowances? Give examples.
13. Mention any two special allowances notified u/s 10 (14) (i) of IT Act.
(Bangalore University, B.Com., Nov/Dec 2015)
14. List any six allowances which are fully taxable.
15. List any six allowances which are fully exempt.
16. What is Dearness Allowance? **(Bangalore University, BBM, Nov/Dec 2014)**
17. What is the provision related to Hostel Allowance?
(Bangalore University, B.Com., Nov/Dec 2015)
18. State the tax treatment for Entertainment Allowance.
19. State the tax provisions relating to House Rent Allowance.
20. What is the tax treatment for Children Education Allowance?
21. How do you treat the children hostel allowance received by an employee?
(Bangalore University, BBM, Nov/Dec 2014)
22. Explain the tax treatment for Hostel Expenditure Allowance.
23. List any six special allowances.
24. What are perquisites? How are they different from Allowances?
25. Give two examples of tax free perquisites. **(Bangalore University, B.Com., Nov/Dec 2015)**
26. List any six tax-free perquisites.
27. Give the meaning of salary for the purpose of calculating exempted RPF contribution by employer.
(Bangalore University, B.Com., Nov/Dec 2016)
28. What does 'family' include, for the purpose of medical benefits?
29. What is 'family' for the purpose of Leave Travel Concession?
30. State the cases where 'rent-free accommodation' is tax-free.
31. State the cases where 'motor-car facility' is tax-free.
32. State the cases where 'interest-free or concessional interest loan' is tax-free.

33. What does 'members of the household' include, for the purpose of perquisites.
34. What is 'Salary' for the purpose of 'rent-free accommodation'?
35. State the tax provision for 'hotel accommodation' provided by employer to employee.
36. Give examples of 'personal obligation of employee met or reimbursed by employer'.
37. How would you determine the taxable value of allotment of sweat equity shares?
38. List the perquisites included under 'Fringe Benefits'.
39. What is the taxable value of 'interest-free or concessional interest loan facility' given to employee?
40. What is the taxable value of 'free or concessional holiday home facility'?
41. State the tax provisions relating to 'Free or Concessional Food Facility' provided to employee.
42. What are the tax provisions for Gifts given to employee?
43. Explain the tax provisions pertaining to credit card facility.
44. Explain the tax provisions pertaining to club facility.
45. Explain briefly the tax treatment for 'movable assets of employer, used by employee'.
46. Explain briefly the tax provisions relating to 'transfer of employer's movable assets to employee'.
47. Who is a 'specified employee'?
48. List the perquisites taxable only in the hands of 'specified employee'.
49. State the conditions to be fulfilled for exempting motor-car facility provided by employer to employee, only for official purposes.
50. What is the 'standard valuation' for motor-car provided by employer, which is used by employee for both official and personal purposes?
51. State the tax provisions for motor car owned by employee, expenses for which are met or reimbursed by employer.
52. Explain the tax provisions for 'domestic servant facility' given to employees.
53. Explain the tax provisions for free or concessional supply of gas, electricity and water.
54. State the tax provisions relating to free or concessional education provided to members of the household of the employee, in an institution run by employer.
55. Explain the tax treatment for free or concessional transport facility provided by a transport undertaking.
56. List the various items included under 'profits in lieu of salary'.
57. State the tax provisions pertaining to 'Retrenchment Compensation'.
58. State the tax treatment for 'voluntary retirement compensation'.

Section B Type Questions

1. Explain the 'Chargeability' and 'Basis of Charge' for 'Income from Salaries', with examples.
2. Explain in brief the tax-treatment for gratuity received at the time of retirement by employees covered under 'Payment of Gratuity Act'.
3. Explain in brief the tax-treatment for gratuity received at the time of retirement by employees who are not covered under 'Payment of Gratuity Act'.
4. Explain the tax provisions for leave salary received at the time of retirement.
5. Explain in detail the tax-treatment for House Rent Allowance.

6. What is Entertainment Allowance? Explain the tax provisions relating to Entertainment Allowance.
7. List the various perquisites taxable in the hands of all employees.
8. Explain in detail the provisions for valuation of 'rent-free accommodation'.
9. Explain in detail the determination of 'fair market value' in computing taxable value of 'allotment of shares under Employee Stock Option Plan'.
10. Explain the provisions for valuation of 'interest-free or concessional interest loan' advanced by employer to employee.
11. Explain the tax provisions for computing taxable value of 'movable assets transferred by employer to employee'.
12. Explain in detail the tax-treatment for motor-car provided by employer to employee.
13. State the conditions to be fulfilled for claiming exemption for 'voluntary retirement compensation' under section 10(10C).

Section C Type Questions

1. Explain in detail the tax provisions for valuation of rent-free accommodation.
2. Explain in detail, the tax-treatment for different fringe benefits.
3. Explain the tax provisions for valuation of motor-car facility provided to employee.
4. Explain the tax-provisions relating to—
 - (i) Medical Benefits.
 - (ii) Leave Travel Concession.

EXERCISES

Section B Type Questions

1. Jagan, a non-government employee, receives ₹3,06,000 as leave salary at the time of retirement on February 20, 2018. On the basis of the following information, determine the amount of taxable leave salary: Basic Pay ₹18,000 per month since 2013, duration of service – 32 years, leave at the credit of Jagan at the time of retirement – 17 months, entitlement of leave salary – 45 days' salary for every year of service and leave availed while in service – 31 months.

(Ans: Taxable Leave Salary – ₹2,88,000)

2. Mr. Srinidhi retires from service on 30/6/2017. He is paid pension of ₹7,500 per month. He commutes 75% of his pension on 1/12/2017 and receives ₹4,50,000 as commuted pension. Compute the taxable amount of commuted pension for the AY 2018-19 assuming that (a) He is a Government Employee, (b) He is not a Government Employee who does not receive gratuity and (c) He is not a Government Employee but receives gratuity.

(Bangalore University, B.Com., Nov/Dec 2014)

(Ans: (a) Nil (b) ₹1,50,000, and (c) ₹2,50,000)

3. Mr. Vinodh retired from services on 31/3/2017. His pension was fixed at ₹16,000 per month. He commutes 3/4th of his pension and receives ₹14,40,000 during the Previous Year 2017-18. Find out the taxable amount of commuted pension when—

- (a) He is a Government Employee

- (b) He is not a Government Employee but is receiving Gratuity
- (c) He is not a Government Employee and is not receiving Gratuity

(Bangalore University, B.Com., Nov/Dec 2012 – Modified)

(Ans: (a) ₹ Nil; (b) ₹ 8,00,000 & (c) ₹ 4,80,000)

4. Mr. Anand is getting a pension of ₹ 12,000 pm from a company. During the PY 2017-18 he got half of pension commuted for ₹ 5,00,000. Compute the exempted amount of commuted pension for the AY 2018-19 if:

- (a) He receives gratuity
- (b) He does not receive any gratuity

(Bangalore University, B.Com., Nov/Dec 2015)

(Ans: (a) ₹ 3,33,333 & (b) ₹ 5,00,000)

5. Mr. Kumar is a non-government employee getting pension of ₹ 16,000 pm from a company. During the PY 2017-18 he got his 2/3rd pension commuted and received ₹ 9,84,000. Compute taxable pension for the AY 2018-19.

(Nov/Dec 2016)

(Ans: ₹ 3,10,000)

Assumptions

- (i) Date of commutation of pension is taken as 01-04-2017.
 - (ii) Kumar is considered as not covered under Payment of Gratuity Act, 1972.
6. Mr. Veeresh retired on 31-03-2018 after serving in a company for 32 years and 10 months. He received ₹ 1,78,000 as gratuity. His average monthly salary in the immediately preceding 10 months was ₹ 28,000. Compute his taxable gratuity for the AY 2018-19 (Gratuity is not covered under Gratuity Act)

(Bangalore University, B.Com., Nov/Dec 2017)

(Ans: ₹ Nil)

7. Venu, an employee of LMN Ltd., receives ₹ 93,000 as gratuity under the Payment of Gratuity Act, 1972. He retires on 1st January 2018 after rendering service of 20 years and 6 months. At the time of retirement monthly salary was ₹ 8,000 (inclusive of dearness allowance of ₹ 200 per month). Calculate amount of gratuity chargeable to tax.

(Ans: Taxable Gratuity – ₹ 692)

8. Rakesh, not being covered by the Payment of Gratuity Act, 1972, retires on January 25, 2018 from PQR and receives ₹ 3,76,000 as gratuity after service of 40 years and 2 months. His average monthly salary during March 1, 2017 to December 31, 2017 is ₹ 16,590. Determine the amount of gratuity exempt and taxable for Assessment Year 2018-19.

(Ans: ₹ Exempted Gratuity – ₹ 79,050 and Taxable Gratuity – ₹ 2,90,950)

9. Mr. Harish, General Manager in a private company in Bengaluru retired from his services on December 15, 2017 after 28 years and 8 months of service and received ₹ 3,50,000 as death-cum-retirement gratuity. At the time of retirement his basic salary was ₹ 18,200 per month. He has received ₹ 1,000 per month as D.A. 80% of which forms part of salary for the purpose of computation of retirement benefits and 6% commission on turnover achieved by him. The total turnover achieved by him for 10 months ended 30th November, 2017 is ₹ 1,50,000. Assume he is not covered under Gratuity Act and compute his taxable gratuity for the AY 2018-19.

(Bangalore University, B.Com., Nov/Dec 2014)

(Ans: Nil)

10. Mr. Vijay Kumar (Resident) is employed at a salary of ₹6,200 per month and DA ₹2,800 per month. He retired from his service on 30/5/2017 after completing 29 years of service. He received ₹2,00,000 as gratuity under the Payment of Gratuity Act. Compute his taxable gratuity for the AY 2018-19.

(Bangalore University, BBM, Nov/Dec 2014)

(Ans: ₹49,423)

11. Suraj, who resides in Pune, gets ₹2,20,000 per annum as basic salary. He receives ₹65,000 per annum as house rent allowance, though he pays ₹60,000 per annum as house rent. Determine the amount of house rent allowance chargeable to tax for the Assessment Year 2018-19.

(Ans: ₹27,000)

12. Mrs. Shruthi resides in Kolkata during the PY 2017-18. She gets ₹12,000 p.a. as Basic Salary. She gets DA at 20% of Basic Salary (enters for all retirement benefits). She has also received commission ₹15,000 calculated as a percentage on turnover. HRA received by her is ₹11,800 but rent paid by her is ₹14,800 pa. Calculate the taxable HRA for the AY 2018-19.

(Bangalore University, BBM, Nov/Dec 2014)

(Ans: ₹Nil)

13. Neeraj, who lives in Mysore, gets ₹4,00,000 per annum as basic salary and ₹90,000 per annum as dearness allowance (one-third of which is part of salary for computation of retirement benefits). During the previous year 2017-18, X has received salary of 11 months; salary of March 2018 is received in April 2018. Besides basic salary, he receives ₹1,76,000 as house rent allowance, though he pays ₹1,80,000 as house rent to the landlord. Calculate the taxable amount of house rent allowance.

(Ans: ₹39,000)

14. Srinivas, a resident of Mandya, receives ₹9,90,000 per annum as basic salary. In addition, he gets ₹2,60,000 per annum as dearness allowance, which does not form part of basic salary, 6 per cent commission on turnover achieved by him (turnover achieved by him during the relevant previous year 2017-18 is ₹80,00,000). And ₹3,00,000 per annum as house rent allowance. He, however, pays ₹2,45,000 per annum as house rent. Determine the quantum of house rent allowance exempt from tax.

(Ans: ₹98,000)

15. Kumar, an employee of BHS Ltd., draws ₹6,00,000 as basic pay, ₹25,000 as dearness allowance (not forming part of salary) and ₹40,000 as bonus. Besides, the company provides a rent-free unfurnished house in Goa. The house is not owned by the company. Determine the taxable value of perquisite for Assessment Year 2018-19 if lease rent of the house is : (a) ₹80,000 per annum, (b) ₹1,48,000 per annum and (c) ₹3,600 per annum.

(Ans: (a) ₹80,000, (b) ₹96,000 and (c) ₹3,600)

16. Sridhar, a sales manager of a paper company at Shimoga, Karnataka (Population 30 lakh as per 2001 census), draws ₹8,70,000 per annum as basic salary. Besides, he gets ₹12,000 per annum as travelling allowance (fully utilised for official purposes), ₹48,000 per annum as bonus, ₹36,000 as special allowance. His employer provides a rent-free furnished house in Shimoga which is owned by the employer. Fair rent of the house is ₹1,20,000 per annum. During the previous year 2017-18, Sridhar has also received ₹30,000 as arrears of bonus of the financial year 2015-16. Determine the value of the perquisite in respect of rent-free house for Assessment Year 2018-19.

(Ans: ₹1,43,100)

9.130 • Income Tax-I

17. Manjunath, a non-government employee, gets the following emoluments during the previous year 2017-18:

Basic salary: ₹4,80,000; Dearness allowance (forming part of salary): ₹24,000; Commission on Sales: ₹30,000, Advance salary of April 2018: ₹40,000; Electricity bills paid by employer on behalf of Manjunath: ₹16,000, and Education allowance: ₹6,200 (for two children who are school students in Delhi).

Besides, the employer provides a rent-free house in Delhi for residential purposes to Manjunath with effect from December 1, 2017. Lease rent is ₹96,000 per annum. Determine the taxable value of the perquisite in respect of the rent-free house for the Assessment Year 2018-19 on the assumption that lease rent for the period ending March 31, 2018 is still unpaid.

(Ans: ₹26,890)

18. Mr. Pramod is an employee of PQR Ltd., Chennai. He draws Basic Salary ₹2,00,000; Dearness Allowance of ₹15,000; Bonus ₹20,000 and Children Education Allowance ₹3,600 (for the education of his daughter) during the PY 2017-18. Besides the above, the company provides him a residential accommodation free of rent. You are required to calculate the taxable value of rent free accommodation for the AY 2018-19 if the house is –

(a) Owned by the company

(b) Leased by the company at a lease rent of ₹20,000 per annum **(Nov/Dec 2010 – Modified)**

(Ans: (a) ₹33,360 & (b) ₹20,000)

19. Mr. Harish resides in Mumbai. During the PY 2017-18 he gets Basic Salary ₹12,000 per month, DA 20%, Medical Allowance ₹300 per month and Special Allowance ₹250 per month. He is provided with a rent-free accommodation. The cost of furniture provided is ₹1,20,000. You are required to compute taxable value of rent free furnished accommodation for the AY 2018-19.

(Bangalore University, B.Com., Nov/Dec 2011 – Modified)

(Ans: ₹34,590)

20. Mr. Nataraj is employed in a town (population 13 lakh). Particulars of his income for the AY 2018-19 are:

Basic Salary ₹16,000 per month

Dearness Allowance ₹4,000 per month (60% does not enter into service benefits)

Entertainment Allowance ₹1,000 per month

Bonus ₹16,000

He has been provided with rent-free accommodation. The cost of furniture provided is ₹2,00,000.

Compute his taxable income from salary for the AY 2018-19.

(Bangalore University, B.Com., Nov/Dec 2012 & 2014 – Modified)

(Ans: ₹55,880)

21. Mr. Raju, a resident of Mysuru, provides the following particulars of his income for the PY 2017-18.

(a) Basic Salary ₹22,000 per month

(b) HRA ₹9,600 per month (Actual rent paid ₹6,000 per month)

(c) DA ₹10,000 per month

(d) Entertainment Allowance ₹800 per month (Actual amount spent ₹1,000 per month)

- (e) Self and Employer's contribution to RPF 14% of Salary
- (f) Small car provided by the employer for both personal and official use and all the expenses are met by the employer.

Compute his taxable income from salary for the AY 2018-19.

(Bangalore University, B.Com., Nov/Dec 2013 – Modified)

(Ans: ₹4,90,080)

22. Mr. Chethan is a production manager of a company in Chennai. His particulars of salary income are:

- Basic Salary ₹15,000 pm
- DA ₹5,000 pm (given under the terms of employment)
- Commission ₹12,000 pa on the turnover achieved
- Bonus ₹4,000 pa
- HRA ₹8,000 pm
- Travelling Allowance ₹800 pm (fully spent for official purpose)
- He lives in a rented house for which he pays ₹9,000 pm as rent

Find out his taxable salary income for the AY 2018-19.

(Bangalore University, B.Com., Nov/Dec 2015)

(Ans: ₹2,69,200)

23. Mr. Chethan, a resident of Kolkata, provides you the following particulars of his income for the PY 2017-18. Compute his taxable income from salary for the AY 2018-19.

- (a) Basic Salary ₹30,000 per month
- (b) DA ₹10,000 per month (given under the terms of service agreement)
- (c) Commission ₹2,000 per month
- (d) Bonus ₹60,000
- (e) HRA ₹16,000 per month (Rent paid ₹18,000 per month)
- (f) Travelling Allowance ₹1,600 per month (fully spent for official purpose)

(Bangalore University, B.Com., Nov/Dec 2015 – Modified)

(Ans: ₹5,88,000)

Section C Type Questions

1. Determine the amount of taxable pension for the Assessment Year 2018-19 in the following cases on the assumption that pension becomes due on the last day of month:
 1. Michael retires from the Indian Economic Service on July 31, 2017 and receives ₹32,000 per month as pension.
 2. Michael retires from the Indian Administrative Service on May 31, 2016. He gets pension ₹29,000 per month up to June 30, 2017. With effect from July 1, 2017 he gets 42 per cent of his pension commuted for ₹4,00,000.
 3. Michael retires from ABC(P) Ltd. in December 2014 and receives pension of ₹11,000 per month up to February 28, 2018 when he dies.
 4. Michael retires from XYZ (P) Ltd. on March 31, 2017. The company pays ₹24,000 per month as pension but does not pay any gratuity. On the request of Michael, XYZ (P) Ltd.

pays ₹6,00,000 in lieu of commutation of 30 per cent of pension with effect from February 1, 2018.

5. What will be the amount of taxable pension if Michael, under the circumstances at (4), receives ₹90,000 as gratuity at the time of retirement?

(Ans: (1) ₹2,56,000, (2) ₹2,38,380, (3) ₹1,21,000, (4) ₹2,73,600 and (5) ₹2,73,600)

2. Amit Sen received the following emoluments during the previous year ending March 31, 2018:

Basic salary: ₹9,00,000, dearness allowance: ₹90,000 (not forming part of salary), bonus: ₹74,000 and commission: ₹40,000.

His employer provides the following perquisites:

A rent-free furnished house in Cochin:

Lease rent of unfurnished house - ₹41,000

Cost of steel furniture provided (written down value ₹12,000, steel furniture is provided throughout the previous year) – ₹14,000.

Rent of furniture (rent is yet to be paid by employer) – ₹17,000.

Motor car expenditure of the employee (reimbursed by employer) – ₹6,000.

Determine the value of the perquisite in respect of rent-free furnished house if:

- Amit Sen is an officer in the Government of West Bengal and ₹18,000 is licence fee of unfurnished house as per the State Government Rules,
- Amit Sen is an Officer of the Indian Airlines, and
- Amit Sen is Managing Director of a Private Company.

What will be the value of perquisite, in all the above cases, if employer charges Amit Sen a rent of ₹40,000 per annum?

(Ans: Value of Rent-free Furnished House – (a) ₹36,400, (b) ₹59,400 and (c) ₹59,400, Value of Accommodation provided at Concessional Rent – (a) Nil (b) ₹19,400 and (c) ₹19,400)

3. During the previous year 2017-18, Gowrisha (44 years) a citizen of India, receives ₹12,00,000 as basic pay; ₹1,80,000 as dearness pay (forming part of basic pay); ₹6,00,000 as bonus; ₹1,86,000 as commission (fixed); ₹24,000 as education allowance for his two children (expenditure on children's education: ₹36,000); and medical allowance: ₹12,000 (expenditure: ₹18,000). His employer contributes ₹1,82,000 towards Provident Fund. Interest credited on May 15, 2017 in the provident fund account at the rate of 11 per cent amounts to ₹2,20,000. His income from other sources is ₹4,50,000. During the previous year 2017-18, Gowrisha makes the following payments/contributions:

- Provident fund contribution: ₹2,20,000.
- Insurance premium on the life of his wife: ₹24,000 (sum assured: ₹40,000, policy was taken in 2008).
- Insurance premium on his own life: ₹6,000 (Due date: March 10, 2018, date of payment: April 5, 2018)
- Debentures of a notified infrastructure company: ₹10,000.

Determine the taxable salary of Gowrisha for the Assessment Year 2018-19 on the assumption that he is a member of–

- Statutory Provident Fund
- Recognised Provident Fund
- Unrecognised Provident Fund

(Ans: (a) ₹21,99,600, (b) ₹22,46,000 and (c) ₹21,99,600)

4. Mrs. Vani (43 Years) received the following incomes from Ramesh Ltd. during the year ending March 31, 2018:

Salary @ ₹30,000 per month	₹3,60,000
Leave travel concession for proceeding on leave (expenditure on air fare: ₹72,000)	₹75,000
Lunch allowance @ ₹3000 per month (expenditure ₹36,000)	₹36,000
Medical allowance (expenditure ₹20,000)	₹24,000
Allowance for purchase and maintenance of uniform for official use (expenditure incurred by Vani: ₹4,000)	₹18,000

Mrs. Vani also enjoyed the following benefits and perquisites:

Free unfurnished flat in Mumbai for which employer is paying a monthly rent of ₹30,000.

Free use of Maruti Car with driver for personal use and official use. Car can also be used by the family members of Vani.

Free service of personal attendant (Salary: ₹12,000) and Sweeper (Salary: ₹18,000).

Free use of employer's DVD player (costs to the employer: ₹32,000, year of purchase 2003-04).

Mrs. Vani's salary and allowances for March 2018, though due one March 31, 2018 were received by her only in April 2018.

Compute Taxable Salary of Mrs. Vani for Assessment Year 2018-19. (Ans: ₹5,67,700)

5. Vinay (age: 34 years) receives the following emoluments during the previous year ending March 31, 2018:

Basic pay	₹5,52,000.
Commission	₹2,60,000.

Free car facility for Vinay and his family members only for private use (expenditure of the employer including normal wear and tear: ₹1,21,000)

Entertainment allowance ₹30,000.

On October 1, 2017, the employer gives a housing loan of ₹11,70,000 @ 2 per cent per annum (payable in 15 years) (SBI lending rate: 10.15 per cent).

Vinay contributes ₹1,60,000 towards recognised provident fund. Determine the taxable salary for Assessment Year 2018-19 if:

(a) Vinay is an employee of VPG, a Partnership firm.

(b) Vinay is an employee of the Punjab Government since 1984.

(Ans: (a) ₹9,63,000 and (b) ₹9,58,000)

6. During the previous year 2018-19, Venkatesh (age: 35 years), a nationalised bank, employee in Surat, receives the following emoluments:

Basic salary: ₹46,000 per month, high cost of living allowance (but not forming part of salary): ₹8,000 per month, overtime allowance: ₹7,500 per month and house rent allowance: ₹9,000 per month (rent paid by him: ₹8,500 per month). Employer-bank contributes 14 per cent of basic salary towards recognised provident fund, Venkatesh makes a contribution of ₹8,000 per month. Interest credited on July 5, 2017 at the rate of 12 per cent in the provident fund account of Venkatesh is ₹11,600. The following perquisites are provided by the bank:

(a) Free holiday home facility at Kullu (expenditure of the employer: ₹61,400);

(b) Free gardener (who is an employee of the bank; annual salary of the gardener being ₹48,000 paid directly by the bank);

9.134 • Income Tax-I

- (c) Free sweeper (who is employed by Venkatesh, annual salary of ₹24,000 is paid by the bank);
- (d) Subsidized telephone (expenditure of the employer: ₹16,000); and
- (e) Ordinary medical facility in a private clinic (expenditure of the employer: ₹18,000)

Compute the taxable salary of Venkatesh for Assessment Year 2018-19. (Ans: ₹9,49,057)

7. Mr. Raju (Age: 67 years), a director of RVIM Ltd., gives the following particulars of his income for the previous year ending March 31, 2018:

Basic Salary: ₹1,45,000 per month.

Bonus: One month's salary.

Commission: Two months' basic salary.

Entertainment allowance: ₹60,000 per annum.

A rent-free unfurnished house has been provided in Chennai, lease rent of the house: ₹5,10,000 per annum.

Employer has provided free use of 1798cc car with driver for official and personal purposes; expenses of the employer: ₹2,80,000 (30 per cent of which is attributable towards official purposes and 20 per cent is attributable towards the journey between office and residence). The employer also provides subsidized tea and snacks (expenditure incurred: ₹12,000) and pays mobile phone bills of Raju (total payment being ₹24,000; bill is in the name of employer and telephone is partly used for office purposes and partly for personal purposes).

Employers' contribution towards recognised provident fund: 15 per cent of basic salary.

Determine taxable salary of Mr. Raju for the assessment year 2018-19.

(Ans: ₹26,62,050)

8. Mr. Nagaraj is employed in a factory at Bengaluru. He is covered under the Payment of Gratuity Act, 1972. He retired on 31st December, 2017 after rendering a service of 34 years. At the time of retirement, the employer paid him a gratuity of ₹2,50,000 and accumulated balance of RPF ₹2,20,000. He is also entitled to a pension of ₹3,000 per month. He commuted half of his pension and received ₹1,35,000 on 1st March, 2018. Following are the other particulars:

- (a) Basic Salary ₹7,000 per month
- (b) Dearness Allowance ₹3,400 per month
- (c) Bonus ₹8,000
- (d) Project Allowance ₹6,000
- (e) House Rent Allowance ₹1,400 per month (Rent paid ₹12,000 per annum)
- (f) His and employer's contribution to RPF ₹9,600

Compute Taxable Income from Salary of Mr. Nagaraju for the AY 2018-19.

(Bangalore University, B.Com., April/May 2000 & Nov/Dec 2007– Modified)

(Ans: ₹2,16,540)

9. Mr. Radhakrishna is an employee of SBI. He furnishes the following details of his income for the PY 2017-18.

- (a) Pay Scale since 1/1/2013 ₹12,500 – 500 – 18,000
- (b) Dearness Allowance 15% of Basic
- (c) Entertainment Allowance ₹250 per month
- (d) Bonus ₹4,000

- (e) Children Education Allowance ₹200 per month per child for 3 children
- (f) Travelling Allowance ₹15,000 (Actual spent for official purpose ₹14,000)
- (g) Reimbursement of medical expenses for medical treatment of self and family members in a private clinic ₹25,000
- (h) Provision of residential accommodation for which the bank is deducting a sum of ₹1,000 per month (Actual rent paid by the bank to the owner of accommodation ₹5,000 per month and cost of furniture provided ₹30,000)
- (i) Self and Bank's contribution to SPF 15% of Salary and Dearness Allowance
- (j) Interest credited to SPF account ₹3,300 at 10% per annum
- (k) Professional tax paid ₹2,400
- (l) Income tax paid ₹8,000
- (m) Health insurance premium paid ₹1,500
- (n) Compute Taxable Income from Salary of Mr. Radhakrishna for the AY 2018-19.

(Bangalore University, B.Com., Nov/Dec 2007– Modified)

(Ans: ₹2,41,470)

10. Ms. Hemamalini, who is a Senior Manager at Maruthi Suzuki, Mumbai provides the following details of her income for the PY 2017-18:

- (a) Basic Salary ₹21,000 per month
- (b) Bonus equal to 2 months basic
- (c) Commission 3% on turnover (Actual turnover achieved ₹50,00,000)
- (d) DA forming part of salary ₹7,000 per month
- (e) Medical Allowance ₹1,400 per month (Actual expenses incurred during the year ₹12,000)
- (f) Entertainment Allowance ₹3,000 per month (Actual expenses incurred during the year ₹30,000)
- (g) Children Hostel Expenditure Allowance ₹500 per month per child for 3 children
- (h) Company's contribution to RPF 6,000 per month
- (i) Interest accrued on RPF at 12% per annum ₹48,000
- (j) Gift of watch worth ₹25,000 from the company on completion of 10 years of service.
- (k) Holiday home facility for her and her family members ₹26,000
- (l) Rent free accommodation for which the company is paying a rent of ₹10,000 per month
- (m) Cost of furniture installed at the above accommodation ₹2,00,000
- (n) Chauffer driven Honda City car above 1,600 cc provided for personal as well as official use. Company owns the car and incurs ₹56,000 towards petrol and ₹36,000 towards driver's salary
- (o) Professional tax paid ₹200 per month

Compute Ms. Hemamalini's taxable income from salary for the AY 2018-19.

(Bangalore University, B.Com., Nov/Dec 2008 – Modified)

(Ans: ₹7,41,620)

11. Mr. Kiran is working in a private company in Bengaluru. From the following details compute his taxable income from salary for the AY 2018-19:

- (a) Net Basic Salary ₹1,44,000 after deduction of tax at source ₹16,000 in the year

- (b) Dearness Allowance ₹1,600 per month (not forming part of salary)
- (c) Bonus equal to 3 months basic salary
- (d) House rent allowance ₹1,600 per month but he is paying a rent of ₹2,400 per month for his residence in Bengaluru
- (e) His son is studying in a residential school in Coorg and the company is paying educational allowance of ₹8,000 and hostel allowance of ₹16,000 yearly
- (f) He is contributing to RPF at 15% of salary and the company is also contributing an equal amount
- (g) Interest earned on RPF ₹8,400 at 14% per annum
- (h) Conveyance Allowance ₹17,000 of which he spent ₹11,000 for official purpose
- (i) He is the member of Lions Club International and the annual membership fees of ₹4,000 is paid by the company
- (j) He has a telephone at his residence for personal and official use and its bill ₹10,000 is paid by the company
- (k) He paid ₹2,400 professional tax

(Bangalore University, B.Com., Nov/Dec 2012 – Modified)

(Ans: ₹2,59,900)

12. Following are the particulars of salary of Mr. Kapoor who works as Managing Director of Royal Airways Ltd., Mumbai. You are required to compute his taxable salary income for the AY 2018-19:

- (a) Basic Salary ₹35,000 per month
- (b) Dearness Allowance 50% of basic salary
- (c) Entertainment Allowance ₹10,000 per month (Actual expenses ₹9,000 per month)
- (d) Rent free furnished house is provided which is owned by the company and its fair value is ₹12,000 per month. Furniture costing ₹2,50,000 is also provided
- (e) Services of the following servants (paid by the company) are provided
 - Watchman ₹1,000 per month
 - Gardner ₹750 per month
 - Sweeper ₹800 per month
 - Cook ₹600 per month
- (f) The company also provided free supply of gas, electricity and water worth ₹18,000 per annum
- (g) The company provides one large car (more than 1,600 cc) with driver for both official and personal purpose. All expenses are met by the company
- (h) He paid professional tax at ₹200 per month.

(Bangalore University, B.Com., Nov/Dec 2012 – Modified)

(Ans: ₹9,40,000)

13. The following particulars relate to the income of Mr. Pavan for the PY 2017-18:

He is employed in a cotton textile mill at Bengaluru on a monthly salary of ₹25,000. He is also entitled to a commission at 1% of sales effected by him. The sales effected by him during the PY amounted to ₹40,00,000. He received the following allowances and perquisites during the PY:

- (a) Dearness pay at ₹6,000 per month

- (b) Bonus at two months basic salary
 - (c) Entertainment allowance at ₹2,000 per month
 - (d) House rent allowance at ₹5,000 per month
 - (e) The employer paid ₹10,000 towards the income tax liability of Mr. Pavan
 - (f) The employer provided a telephone at his residence by meeting all expenses amounting to ₹6,000 for the year
 - (g) He and his employer contributed 15% of his salary to his RPF and interest credited to this fund at 10% amounted to ₹30,000 during the PY
 - (h) He spent ₹6,000 per month as rent of the house occupied by him in Bengaluru.
- Compute his taxable income under the head salaries for the AY 2018-19.

(Bangalore University, B.Com., Nov/Dec 2014)

(Ans: ₹5,39,060)

14. Mr. Ganesh, Manager of Maruthi Suzuki Ltd., Mumbai has furnished the following details of his income for the year ended 31st March, 2018:

- (a) Basic salary ₹21,000 per month
- (b) Bonus – 2 months basic
- (c) Commission – 3% on sales. During the year he reached a sales of ₹5,00,000
- (d) Dearness allowance forming part of salary ₹7,000 per month (considered to retirement benefits)
- (e) Medical allowance ₹1,400 per month
- (f) Entertainment allowance ₹3,000 per month
- (g) Children's hostel allowance for his two children at ₹500 per month per child
- (h) RPF – Company's contribution ₹6,000 per month
- (i) RPF – Own contribution ₹5,000 per month
- (j) Interest on RPF at 11% per annum ₹44,000

He has been provided rent free furnished accommodation at Mumbai whose fair rental value is ₹10,000 and cost of furniture ₹60,000. He paid professional tax of ₹2,400. Compute his taxable salary for the AY 2018-19.

(Bangalore University, B.Com., Nov/Dec 2014)

(Ans: ₹5,57,670)

15. Mrs. Shruthi who is an officer in XYZ Ltd., gives you the following particulars:

- (a) Basic Salary ₹16,000 per month
- (b) DA ₹1,000 per month (50% enters into retirement benefits)
- (c) HRA ₹5,000 per month (Rent paid ₹7,000 per month at Bengaluru)
- (d) Conveyance Allowance ₹800 per month (₹600 used for official purposes)
- (e) CCA ₹150 per month
- (f) Motor car of above 1,600 CC with driver provided used partly for official and partly for personal purpose
- (g) Children education allowance ₹200 per month per child for 3 children
- (h) Services of sweeper (salary ₹200 per month)
- (i) Payment of her LIC premium ₹8,000 by the company

- (j) She contributes 14% of her salary to RPF and the company makes a matching contribution to RPF. Interest credited to RPF ₹6,875 at 12.5% per annum
Compute her Income from Salary for the AY 2018-19.

(Bangalore University, BBM, Nov/Dec 2014)

(Ans: ₹2,68,610)

16. Sri Sudeep, Sales Manager at ANZ Ltd., Mumbai has furnished the following details of his income for the year ended 31st March 2018:

- (a) Basic Salary ₹17,500 pm
 - (b) DA ₹6,000 pm (forming part of salary)
 - (c) Commission is 2% on sales. During the PY sales target reached by him is ₹4,00,000
 - (d) Bonus equal to 3 months basic salary
 - (e) Entertainment allowance ₹2,500 pm (amount spent ₹12,000)
 - (f) Children Hostel Allowance for his three children ₹400 per month per child
 - (g) Reimbursement of medical bills ₹22,000 for the treatment taken in a private nursing home
 - (h) He is provided with a rent free furnished accommodation owned by the company. The cost of furniture provided is ₹1,00,000 and FRV of the accommodation is ₹7,500 pm
 - (i) Free telephone at his residence for both official and personal purpose ₹3,500
 - (j) Mediclaim Insurance of Mr. Sudeep paid by the company ₹4,000 pa
 - (k) Employment tax paid by the company ₹1,000 pa
 - (l) LIC insurance premium paid by the company ₹1,500 pa on behalf of Sudeep
- Compute his taxable income from salary for the AY 2018-19.

(Bangalore University, B.Com., Nov/Dec 2015)

(Ans: ₹4,59,155)

17. Sri Krishna, an employee of a Transport Company, Bengaluru submits the following information relevant for the AY 2018-19:

- (a) Basic salary ₹8,000 pm
- (b) Conveyance allowance (60% spent for official purpose) ₹2,000 pm
- (c) City compensatory allowance ₹300 pm
- (d) Bonus ₹10,000 pa
- (e) DA ₹1,500 pm (does not form part of salary)
- (f) HRA ₹5,000 pm (Rent paid ₹7,000 pm)
- (g) Payment of LIC premium by the company ₹4,000 pa
- (h) Services of sweeper paid by the company ₹200 pm
- (i) Leave travel concession ₹10,000 (first time in the current block period)
- (j) Reimbursement of gas, electricity and water bill by the company ₹2,500 pa
- (k) Own contribution and company's contribution to the RPF is 14% of salary
- (l) Interest credited to RPF at 14% ₹14,000
- (m) Gift worth ₹10,000 during festival season received from the company during the PY
- (n) Compute his taxable income from salary.

(Bangalore University, B.Com., Nov/Dec 2015)

(Ans: ₹1,79,120)

18. Mrs. Smitha is working as Sales Executive in Maruthi Suzuki Ltd., Kolkata and her salary details are as follows for the PY 2017-18:

- (a) Basic salary ₹21,000 pm
 - (b) Bonus equal to two months basic salary
 - (c) Commission at 3% on sales (During the year she has reached sales target of ₹5,00,000)
 - (d) Dearness Allowance ₹7,000 pm (eligible for retirement benefits)
 - (e) Medical allowance ₹1,400 pm (Medical expenses ₹15,000 pa)
 - (f) Children Hostel Allowance for her two children at ₹500 pm per child
 - (g) Children Education Allowance for her two children at ₹400 pm per child
 - (h) RPF contribution by the company ₹6,000 pm
 - (i) RPF contribution by the employee ₹5,000 pm
 - (j) Interest credited on RPF at 11% ₹44,000
 - (k) She has been provided with company's owned rent-free furnished house in Kolkata and cost of furniture provided is ₹60,000
 - (l) Mrs. Smitha has paid her professional tax ₹2,400 pa
- Compute Taxable Salary for the AY 2018-19.

(Bangalore University, B.Com., Nov/Dec 2016)

(Ans: ₹5,24,550)

19. Mr. Yadav is an employee of State Bank of India, Bengaluru and he submits the following information relevant for the AY 2018-19:

- (a) Basic salary ₹8,000 pm
- (b) Dearness allowance ₹1,500 pm (does not form part of salary)
- (c) City compensatory allowance ₹300 pm
- (d) Bonus ₹10,000 pa
- (e) Conveyance allowance ₹2,000 pm (60% spent for office duties)
- (f) House rent allowance ₹5,000 pm (rent paid by Yadav ₹7,000 pm)
- (g) Payment of LIC premium by SBI ₹4,000 pa
- (h) Services of sweeper paid by SBI ₹200 pm
- (i) Leave Travel Concession ₹5,000 (first time in current block period)
- (j) Reimbursement of gas, electricity and water bills by the SBI ₹2,500 pa
- (k) SPF contribution by the bank and own contribution of Yadav 12% of salary
- (l) Interest credited to SPF at 7% ₹14,000
- (m) Professional tax paid by Yadav ₹5,000
- (n) Compute his taxable income from salary.

(Bangalore University, B.Com., Nov/Dec 2016)

(Ans: ₹1,62,700)

20. Mr. Pratham, Sales Manager of XYZ Ltd., Mumbai has furnished the following details of his income for the year ended 31/03/2018. Compute his income from salary for the AY 2018-19.

- (a) Basic salary ₹20,000 pm
- (b) Dearness allowance ₹6,000 pm (forming part of salary)
- (c) Bonus equal to 3 months basic salary

9.140 • Income Tax - I

- (d) Entertainment allowance ₹2,500 pm (amount spent ₹12,000)
- (e) Children hostel allowance for his three children ₹400 pm per child
- (f) Reimbursement of medical bills ₹22,000 for the treatment taken in a private nursing home
- (g) He is provided with rent-free furnished accommodation owned by the company. Cost of furniture ₹1,00,000. FRV of the house is ₹7,500 pm
- (h) Free telephone at his residence ₹3,500
- (i) Medical insurance premium of Mr. Pratham paid by the company ₹4,000 pa
- (j) Own contribution and company's contribution to RPF is 14% of salary. Interest credited to RPF at 14% pa is ₹14,000

(Bangalore University, B.Com., Nov/Dec 2017)

(Ans: ₹5,02,320)

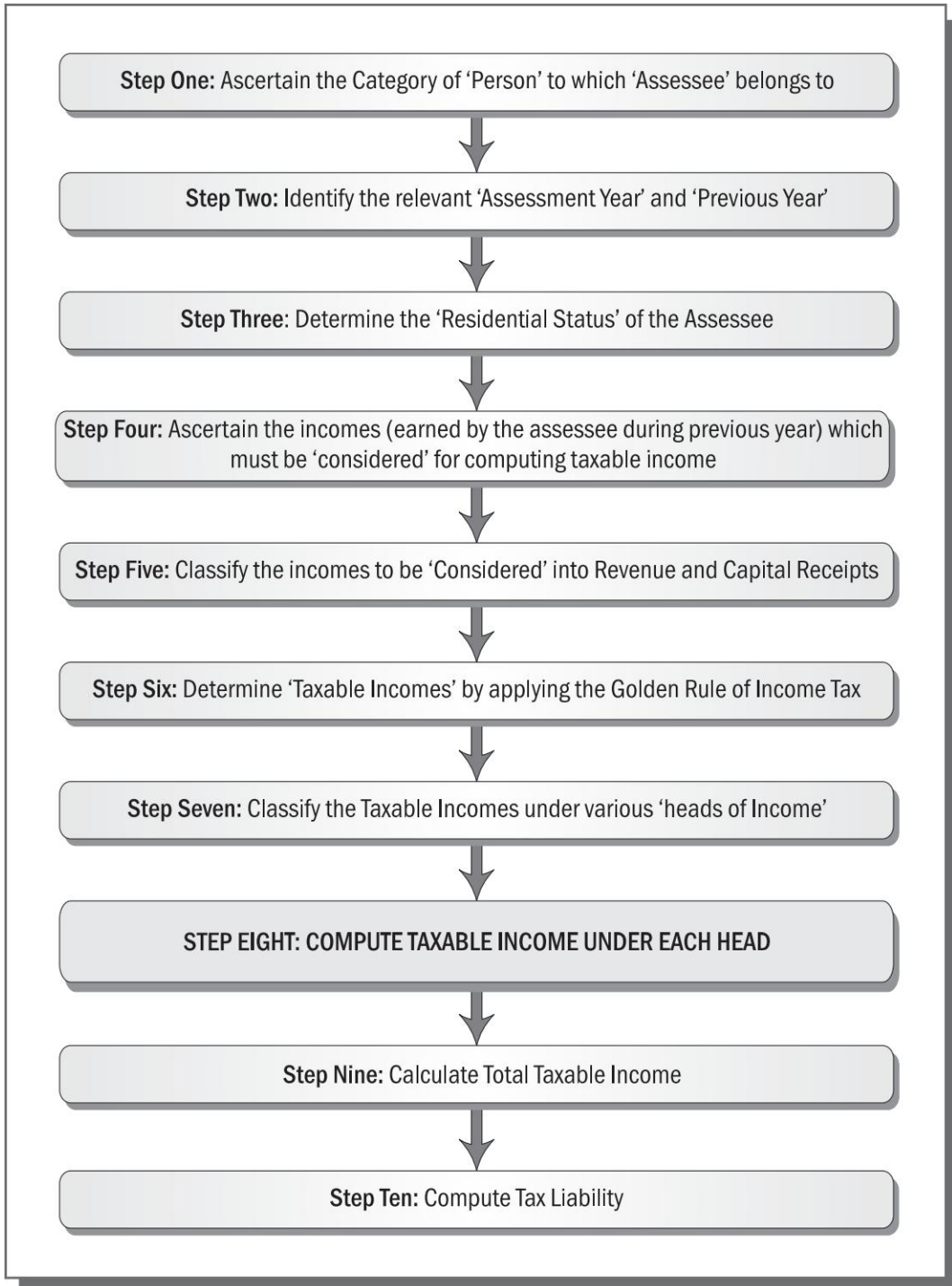
21. The following particulars relate to the income of Mr. Ganesh for the PY 2017-18. He is employed in a Cotton Textile Mill at Bengaluru on a monthly salary of ₹25,000. He is also entitled to a commission at 1% on sales effected by him. The sales effected by him during the previous year amounted to ₹40,00,000. He received the following during the previous year:

- (a) Dearness pay ₹6,000 pm
- (b) Bonus at two months basic salary
- (c) Entertainment allowance ₹2,000 pm
- (d) House rent allowance ₹5,000 pm
- (e) Income tax of Mr. Ganesh paid by employer ₹10,000
- (f) Free telephone installed at his residence ₹6,000
- (g) He and his employer contribute 15% of his salary to his RPF and interest credited to RPF at 10% amounted to ₹30,000 during the year
- (h) He paid ₹6,000 pm as rent of the house occupied by him

Compute his income from salary for the AY 2018-19.

(Bangalore University, B.Com., Nov/Dec 2017)

(Ans: ₹5,39,060)



Income from House Property

CHAPTER OVERVIEW

- 10.1 Chargeability
- 10.2 Basis of Charge
- 10.3 Formats and Provisions
- 10.4 Special Provisions under the Head 'Income from House Property'

- In the process of making assessment, the next step is to compute taxable income under each 'head of income'. This chapter explains computation of taxable income under the second head – "Income from House Property".

CHARGEABILITY

10.1

According to Section 22 of the Income Tax Act, 1961, an income is chargeable under the head "Income from House Property" when the income is from a 'property' which **can be considered** under the head 'house property'.

A 'Property' **can be considered** under the head 'House Property' when the following conditions are fulfilled—

- (a) The property should consist of any buildings or lands appurtenant thereto;
- (b) The assessee should be the owner of the property;
- (c) The property should not be used by the owner for the purpose of any business or profession carried on by him, the profits of which are chargeable to income-tax.

Notes:

1. In this case, the conditions are applicable for the 'property' than the 'income'.
2. The **first condition** for considering a 'property' under "House Property" is that the property must not be some property (like car, jewelry, etc.,) but must be a 'house property'. Under the Income Tax Act, 'House Property' means 'property consisting of buildings or land appurtenant thereto'.

10.4 • Income Tax - I

3. 'Building' means 'enclosure of walls – with or without a roof'. Accordingly, a residential house, a commercial complex, an office building, a godown, swimming pool, stadium, lecture halls, convention centers etc., are buildings.
4. 'Land appurtenant' to the building means the land which is an indivisible part of the building for its use and enjoyment by the occupiers and the land is not put to any other use and is not yielding any income assessable under the head other than "income from house property". It includes approach roads to and from the building, parking space, garden, kitchen garden, corridors, cattle-shed, space between compound wall and the main building, etc.
5. Only when a property consists of 'building and land appurtenant thereto', it can be considered as 'House Property'. So, income from letting vacant land is not 'income from house property' since there is no building. A House boat is not a 'House Property' since it does not have land appurtenant thereto.
6. The **second condition** for considering a 'property' under the head 'house property' is that the property must be owned by the assessee. The ownership may be legal ownership or true ownership.
7. If title of ownership of a house property is under dispute in a court of law, the decision about who is owner rests with the Income-tax Department. Generally, the person who is in receipt of income or the person who enjoys the possession of a house property as owner is assessable to tax.
8. According to Section 27 of the Income Tax Act, 1961, the following are the situations where the assessee is not the 'legal owner' yet will be **deemed** (i.e., treated) as owner of the property:
 - (a) A person who has transferred property to Spouse or Minor Child without adequate consideration.

Where an individual transfers a house property to his or her spouse without adequate consideration and not for an agreement to live apart, then the transferor individual will be deemed to be owner of the property, although the transferee individual is the legal owner.

Similarly, when an individual transfers a house property to his or her minor child (*other than minor married daughter*), without adequate consideration, then the transferor will be deemed to be owner of the property, although the child is the legal owner.
 - (b) Holder of an Impartible Estate

Where a house property is owned by more than one person, but the share of each partner is *unknown or unascertainable*, then for tax purposes, the holder of the property will be deemed to be the owner of the property.
 - (c) Property held by a Member of Co-operative Society or Company or Association of Persons, who has been allotted with the property under any Housing Scheme of the Society or Company or AOP.

When a member has been allotted a house property under a Housing Scheme by a Cooperative Society or Company or Association of Persons – then the member, to whom the property is allotted will be deemed to be the owner of the property, for tax purposes, although the ownership remains with the Society till the member settles the entire consideration of the allotted property.

(d) A person who has acquired property under a Power of Attorney Transaction.

Where a sale of property has taken place between two parties, then the buyer will be deemed to be the owner of the property if, the possession of property is given by seller to buyer, the buyer has paid the consideration or has kept it ready for payment, however, the registration in the name of buyer has not been effected. Then, the buyer is said to be having a 'Power of Attorney' on the property and will be deemed to be the owner of the house property.

(e) A person who has acquired a property on lease for a term of 12 years or more.

When a property is leased by one person to another, for a period of 12 years or more, then the lessee will be deemed to be the owner of the property, for tax purposes.

9. When a tenant of a property sub-lets the property and earns rental income, it is not 'income from house property' since the tenant is not the 'owner of the property'.
10. The **third condition** states that the house property owned by the assessee must not be used by the assessee for any business or profession carried on by him as a **proprietor**, or by a firm in which he is a **partner**.
11. Where a house property owned by the assessee is let out by him to the employees of the business carried on by him, the income from such property is 'Income from House Property' when such letting out is **not** subservient and incidental to the business of the assessee. However, where such letting out is subservient and incidental to the business of the assessee, income from letting out property to employees is charged under the head 'income from business or profession'.
12. Where the premises of the assessee is given to any Government agency for locating a branch of a bank, police station, excise office, post-office, railways, etc., for the purpose of running the **business of the assessee** more efficiently and smoothly (and not with the main intention of earning rental income), then the premises must be considered as property used by the assessee for his business and hence, the income from such property must be considered under the head 'income from business'.
13. Where the assessee is engaged in real-estate business, any income derived from a property held as stock-in-trade must be considered under the head 'Income from House Property' and not under 'Income from Business' since the property is **not used in** the business carried on by the assessee.
14. Where the assessee is engaged in the **business of letting out** properties, income from such properties must be assessed under the head 'Income from House Property' and not under the head 'Income from Business'.

15. Where the assessee is in the business of providing 'paying guest accommodation' which involves not only providing of accommodation, but also providing food and other services, then the income derived must be considered as 'Income from Business', since the income is derived not from mere ownership of the house property, but because of facilities and services rendered.

10.1.1 Cases where Property Income is not Chargeable to Tax

In the following cases, income from house property is exempt from tax:

- (a) Income from farm house. [Sec 10(1)]
- (b) Annual value of any one palace of an ex-ruler. [Sec 10(19A)]
- (c) Property income of a local authority. [Sec 10(20)]
- (d) Property income of an approved scientific research association. [Sec 10(21)]
- (e) Property income of an educational institution and hospital. [Sec 10(23C)]
- (f) Property income of a trade union. [Sec 10(24)]
- (g) House property held for charitable purposes. [Sec 11]
- (h) Property income of a political party. [Sec 13A]

BASIS OF CHARGE

10.2

Computation of income taxable under the head 'income from house property' depends on the '**nature of occupation**' of the property. That is, the taxable income under this head must be calculated on the basis of the purpose for which the property is used by the assessee. Hence, 'nature of occupation' is considered as the basis of charge.

On the basis of 'nature of occupation', house properties are classified into the following types:

1. Let-out Property (for residential or commercial purposes).
2. Self-occupied Property (for residential purposes).
3. Deemed to be let out Property.
4. Partly let-out and partly self-occupied property.

FORMATS AND PROVISIONS

10.3

The format for each of the above listed type of property and the provisions are explained in detail, below:

10.3.1 Let-Out Property

Let-out property refers to property given on rent. The tenant might use the property for residential or commercial purpose. For tax provisions, the purpose for which the tenant is using the property is irrelevant.

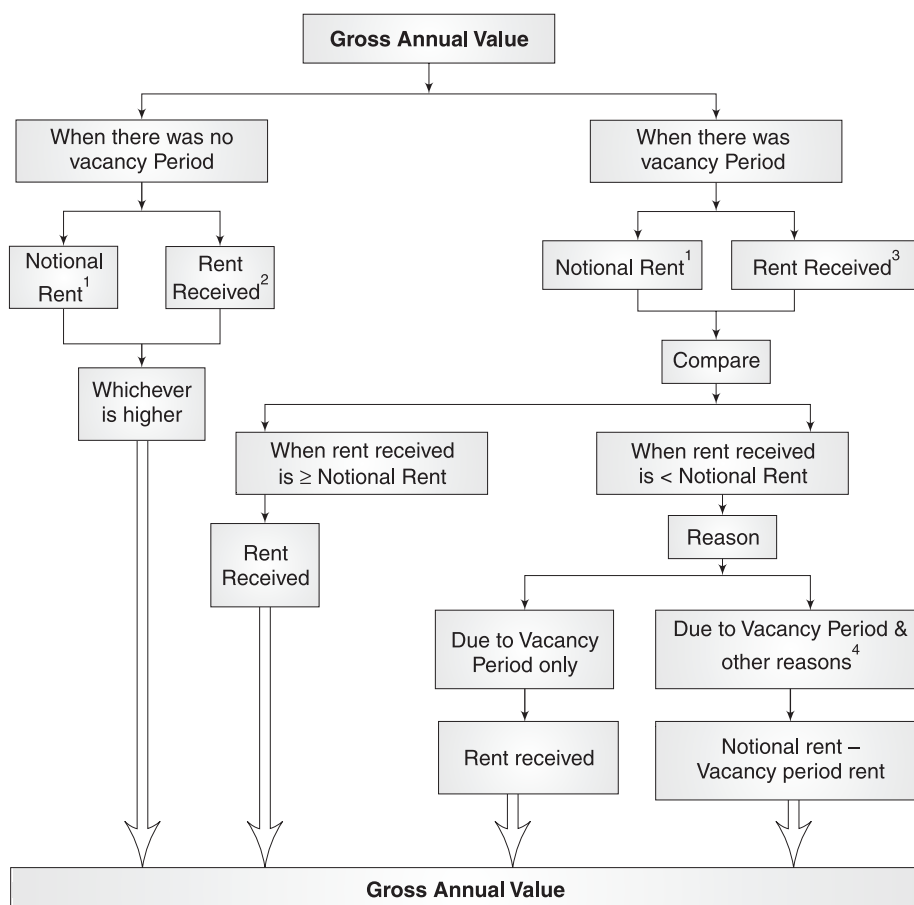
The format for computing taxable income from a ‘let-out house property’, and the provisions for the same, are as follows–

	₹	₹
Gross Annual Value		XXX
Less: Municipal Taxes <i>paid</i> by the <i>assessee</i> during the <i>previous year</i> .		XXX
Net Annual Value		XXX
Less: Deductions under section 24		
Standard Deduction	XXX	
Interest on Borrowed Capital	XXX	XXX
Income From Let-out Property		XXX

Gross Annual Value

According to Section 23(1)(a), the annual value of a property shall be the sum for which the property might reasonably be expected to be let from year to year.

The following flow-chart summarises the provisions for calculation of ‘Gross Annual Value’ for a let-out property:



Notes:

1. Notional rent is higher of municipal value and fair rental value, restricted to standard rent.
2. Rent received (when there is no vacancy period) = Annual rent *minus* unrealised rent (if all required conditions for its deduction are satisfied).
3. Rent received (when there is vacancy period) = Annual rent *minus* unrealised rent (if all required conditions for its deduction are satisfied) *minus* vacancy period rent.
4. Apart from vacancy period, the other reasons due to which rent received can be lower than notional rent, are:
 - (a) Annual rent being less than notional rent.
 - (b) Annual rent *minus* unrealised rent, being less than notional rent.

An **alternative approach** to calculate Gross Annual Value is as follows:

	₹
Step 1: Calculation of Notional Rent	
Higher of Municipal Value and Fair Rental Value restricted to Standard Rent	XXXX
Step 2: Calculation of Rent Recovered	
Annual Rent minus Unrealized Rent	XXXX
Step 3: Calculation of Gross Annual Value	
Higher of Step 1 and Step 2 minus Vacancy Period Rent	XXXX

The following are required for calculating Gross Annual Value:

1. Municipal Value
2. Fair Rental Value
3. Standard Rent
4. Actual Rent
5. Unrealised Rent
6. Vacancy Period Rent

1. *Municipal Value*

It refers to the value of the property as determined by the Municipal Authorities. The Municipal Authorities value every property in its jurisdiction each year, for levy of municipal taxes.

2. *Fair Rental Value*

It refers to the rent of a similar accommodation in same locality. For example, the rent for a 2 BHK in M G Road may be ₹25,000 per month; the rent for a 3 BHK in Commercial Street might be ₹40,000 per month. Such estimate of the rent for a similar accommodation of the assessee is Fair Rental Value.

3. *Standard Rent*

It refers to the rent according to Rent Control Act. Where this Act is applicable, the rent for property in the jurisdiction will be governed by the provisions of the Act. Presently, in India, this Act is applicable only in a few cities.

4. *Actual Rent*

It refers to the actual rent charged by the assessee to the tenant, for letting out his property. The Actual rent must always be considered for the entire period of previous year, while calculating Gross Annual Value. Hence, it is also called 'Annual Rent'.

5. *Unrealised Rent*

It refers to rent not realised from the tenant. Rent not realised or not recovered **can be deducted** while calculating Gross Annual Value, only when the following **conditions** are fulfilled:

- (a) The tenancy is bona fide.
- (b) The tenant has defaulted payment of rent.
- (c) Necessary steps must be taken to vacate the defaulting tenant from the property.
- (d) The defaulting tenant must not be residing in any other property of the assessee.
- (e) All steps have been taken for recovering the rent from the tenant, including legal proceedings; or the defaulting tenant is not available for taking any action.

6. *Vacancy Period Rent*

Where the property was not let out for the entire period of the relevant previous year, then there is said to be a vacancy period during the previous year. Rent for the period during which the property was vacant during the previous year is 'vacancy period rent'. For example, suppose assessee let out the property till January 2018 and the property is vacant from February 2018. If the Actual rent per month is ₹ 10,000, then vacancy period rent is $(₹ 10,000 \times 2) = ₹ 20,000$.

Note: Where the house property is held as stock-in-trade and the property is not let during the whole or any part of the previous year, the annual value of such property shall be taken as 'Nil' (**with effect from Assessment Year 2018-19**). However this concession is available only for the period up to 1 year from the end of the financial year in which the certificate of completion of construction of the property is obtained from the competent authority.

Illustration 1 **Problem on Calculation of Notional Rent**

Calculate Notional Rent for the following properties:

	House A ₹	House B ₹	House C ₹
Municipal Value	2,00,000	2,00,000	2,00,000
Fair Rent	1,96,000	2,04,000	2,04,000
Standard Rent	1,92,000	N.A.	2,08,000

Solution:**Calculation of Gross Annual Value**

	House A ₹	House B ₹	House C ₹
Higher of Municipal Value and Fair Rental Value	2,00,000	2,04,000	2,04,000
Standard Rent	1,92,000	Not Applicable	2,08,000
Notional Rent (Lower of the above two)	1,92,000	2,04,000	2,04,000

Note: Where Rent Control Act is not applicable, the Standard Rent is not available. When Standard Rent is not applicable or available, higher of municipal value and fair rental value, will be Notional Rent or Expected Rent.

Illustration 2 Problem on Calculation of Gross Annual Value when there is no unrealised rent and vacancy period rent

Calculate Gross Annual Value from the following information:

	Property A ₹	Property B ₹	Property C ₹	Property D ₹
Municipal Value	5,00,000	4,50,000	5,00,000	4,00,000
Fair Rent	4,80,000	4,80,000	5,40,000	4,20,000
Standard Rent	5,40,000	4,20,000	4,80,000	4,50,000
Annual Rent	4,80,000	3,60,000	4,50,000	4,80,000

Solution:**Calculation of Gross Annual Value**

	Property A ₹	Property B ₹	Property C ₹	Property D ₹
Step One – Calculation of Notional Rent (Higher of Municipal Value and Fair Rental Value, restricted to Standard Rent)	5,00,000	4,20,000	4,80,000	4,20,000
Step Two – Calculation of Rent Recovered (Annual Rent <i>less</i> Unrealised Rent)	4,80,000	3,60,000	4,50,000	4,80,000
Step Three – Calculation of Gross Annual Value (Higher of Steps 1 and 2 <i>minus</i> Vacancy period rent)	5,00,000	4,20,000	4,80,000	4,80,000

Illustration 3 Problem on Calculation of Gross Annual Value when there is unrealised rent

Calculate Gross Annual Value for the following properties:

	Property I ₹	Property II ₹	Property III ₹	Property IV ₹
Municipal Value	8,00,000	10,00,000	5,00,000	7,00,000
Fair Rent	8,40,000	9,60,000	6,00,000	7,20,000
Standard Rent	NA	10,20,000	5,40,000	9,60,000
Annual Rent	9,60,000	9,60,000	6,00,000	8,40,000
Unrealised Rent	1,60,000	80,000	1,00,000	70,000

Solution:

Calculation of Gross Annual Value

	Property A ₹	Property B ₹	Property C ₹	Property D ₹
Step One – Calculation of Notional Rent (Higher of Municipal Value and Fair Rental Value, restricted to Standard Rent)	8,40,000	10,00,000	5,40,000	7,20,000
Step Two – Calculation of Rent Recovered (Annual Rent <i>less</i> Unrealised Rent)	8,00,000	8,80,000	5,00,000	7,70,000
Step Three – Calculation of Gross Annual Value (Higher of Steps 1 and 2 <i>minus</i> Vacancy period rent)	8,40,000	10,00,000	5,40,000	7,70,000

Illustration 4 Problem on Calculation of Gross Annual Value when there is unrealised rent and vacancy period

Calculate Gross Annual Value for the following properties:

	Property I ₹	Property II ₹	Property III ₹	Property IV ₹
Municipal Value	8,00,000	14,00,000	10,00,000	7,50,000
Fair Rent	9,60,000	12,00,000	9,60,000	8,40,000
Standard Rent	9,00,000	18,00,000	12,00,000	7,20,000
Annual Rent	9,00,000	16,20,000	12,00,000	6,60,000
Unrealised Rent	75,000	1,00,000	1,00,000	60,000
Vacancy Period	2 Months	1 Month	3 Months	1 Month

Solution:**Calculation of Gross Annual Value**

	Property A ₹	Property B ₹	Property C ₹	Property D ₹
Step 1 – Calculation of Notional Rent (Higher of Municipal Value and Fair Rental Value, restricted to Standard Rent)	9,00,000	14,00,000	10,00,000	7,20,000
Step 2 – Calculation of Rent Recovered (Annual Rent <i>less</i> Un-realised Rent)	8,25,000	15,20,000	11,00,000	6,00,000
Step 3 – Calculation of Gross Annual Value (Higher of Steps 1 and 2 <i>minus</i> Vacancy period rent)	9,00,000 (–) $[2/12 \times 9,00,000]$ = 8,50,000	15,20,000 (–) $[1/12 \times 16,20,000]$ = 13,85,000	11,00,000 (–) $[3/12 \times 12,00,000]$ = 8,00,000	7,20,000 (–) $[1/12 \times 6,60,000]$ = 6,65,000

Municipal Taxes

Municipal Taxes refer to taxes levied by the local authority on the property. It is levied in various names like water cess, sweeper cess, sewerage maintenance cess, halalkore tax etc. Municipal Tax is levied as a **percentage** of municipal value of the property.

Municipal Taxes can be deducted from Gross Annual Value, when the following conditions are fulfilled:

- it must be paid,
- by the owner (i.e., assessee),
- during relevant previous year.

When any of the above conditions are not fulfilled, municipal taxes cannot be deducted. So, municipal taxes levied but yet to be paid are not deductible. Municipal taxes of a property paid by tenant of the property, or any person other than the owner of the property are not deductible.

Municipal taxes are deductible on payment basis. That is, only amount paid during relevant previous year is deductible, irrespective of the period to which the taxes paid belongs to. The entire amount of municipal tax **paid** during previous year must be deducted.

When Municipal taxes paid by the assessee during previous year is deducted from Gross Annual Value, we arrive at '**Net Annual Value**'.

Where, the deduction for municipal taxes exceeds gross annual value, the 'Net Annual Value' will be **negative**. Although, negative value of a property does not connote any meaning, for tax purposes, the same should be considered.

Illustration 5 Problem on Calculation of Net Annual Value for a let-out property

Find Net Annual Value for assessment year 2018-19:

PARTICULARS	₹
Municipal Value	1,20,000
Fair Rent	1,30,000
Standard Rent	1,10,000
Actual Rent, if property is let out throughout the previous year	1,26,000
Unrealised rent of previous year	10,500
Vacancy period	1 month
Municipal tax paid by owner in the previous year	17,000
Municipal tax of previous year paid after 31-03-2018	1,000
Municipal tax paid by the tenant in the previous year	6,000

Solution:**Computation of Net Annual Value**

	₹	₹
Gross Annual Value (See Note No. 1)		1,05,000
Less: Municipal Taxes <i>paid</i> by the <i>assessee</i> during the <i>previous year</i> .		17,000
Net Annual Value		88,000

Notes:

1. Calculation of Gross Annual Value

	₹
Step One – Calculation of Notional Rent (Higher of Municipal Value and Fair Rental Value, restricted to Standard Rent)	1,10,000
Step Two – Calculation of Rent Recovered (Annual Rent <i>less</i> Unrealised Rent)	1,26,000 (–) 10,500 = 1,15,500
Step Three – Calculation of Gross Annual Value (Higher of Steps 1 and 2 <i>minus</i> Vacancy period rent)	1,15,500 (–) [1/12 × 1,26,000] = 1,05,000

2. Municipal taxes paid by tenant are not deductible. The amount of tax paid after 31st March 2018 is not deductible for previous year 2017-18. However, it can be deducted for previous year 2018-19.

Deductions under Section 24

From Net Annual Value of a let out property, when deductions under section 24 are provided, we arrive at 'Income from Let-out Property'. There are two deductions under section 24, viz.,

- (a) Standard deduction.
- (b) Interest on borrowed capital

Standard Deduction [Section 24(a)]

It is a deduction for the expenses incurred by the owner on the property for repairs, maintenance, insurance, taxes levied by other authorities like State Government, rent collection charges in case of let-out property, etc. However, the actual expenditure incurred by the assessee is not deducted, and instead a standard deduction is prescribed. The standard deduction is available irrespective of whether the assessee incurs any expenditure towards the property or not, and the quantum of expenditure incurred, if any.

The standard deduction is – **30% of 'Net Annual Value'**.

Where the Net Annual Value is negative, standard deduction must be taken as 'Nil'.

Interest on borrowed capital [Section 24(b)]

Under this clause, deduction is available for interest on loan borrowed by the assessee for **property** purposes. That is, where the assessee had borrowed any loan for purchase, construction, alteration, modification, repairs, renewals or reconstruction of property, then the interest on such loan is deductible under section 24(b).

Suppose, an assessee has borrowed a loan for his daughter's marriage, by mortgaging his house property. Interest on such loan is not deductible, though property is involved in borrowing, since the loan is not borrowed for property purposes.

The amount of interest deductible is calculated in the following manner:

	₹
Previous Year Interest	XXX
Add: One-fifth of 'Pre-completion period interest'	XXX
	XXX

Previous Year Interest refers to interest on loan outstanding for the relevant previous year.

'Pre-Completion period interest' refers to interest for 'pre-completion period'. 'Pre-completion period' is the period commencing from the date of borrowing the loan and ending on **earlier** of 31st March preceding the date of completion of construction, **or** date on which the loan has been completely repaid. The pre-completion period interest must be **deducted equally over a period of five consecutive years**, commencing from the previous year in which the **construction** of property was **completed**.

Following are the steps involved in ascertainment of pre-completion period:

- (i) Ascertain the date of borrowing the loan.

- (ii) Ascertain the date of completion and identify 31st March immediately preceding that date.
- (iii) Ascertain the date on which the loan has been completely repaid.
- (iv) Consider the **earlier** date among (ii) and (iii).
- (v) The duration between (i) and (iv) is pre-completion period.

For example, suppose assessee borrowed a loan of ₹20,00,0000 for construction of a house property on 1st November 2014. The construction of the property is completed on 18th September 2017. Then, 'pre-completion period' will be from 1st November 2014 till 31st March 2017.

Since, the construction is completed during previous year 2017-18, interest for the entire period of 2017-18 will be considered as 'previous year interest' for 2017-18. Hence, for ascertaining 'pre-completion period', only the duration till 31st March preceding the date of completion of construction is considered.

Suppose, in the above example, assessee had repaid the entire loan by 31st December 2016, then, 'pre-completion period' will be from 1st November 2014 till 31st December 2016.

Since the construction is completed during previous year 2017-18, the pre-completion period interest must be deducted equally over a period of five years commencing from previous year 2017-18. That is, it must be deducted during previous year 2017-18, 2018-19, 2019-20, 2020-21 and 2021-22.

Where the five-year period has expired before the commencement of relevant previous year for the assessee, deduction for pre-completion period interest must not be given.

Notes:

1. Deduction under section 24(b) for interest on borrowed capital is on '**accrual**' basis. That is, the interest amount pertaining to the relevant previous year can be completely deducted, whether it has been paid or not.
2. Interest on **unpaid interest** is not deductible.
3. Where a new loan has been borrowed to repay an earlier housing loan, interest on **new loan** is deductible.
4. Interest on loan borrowed to pay **municipal taxes** is not deductible.
5. Interest paid **outside India** without deducting tax at source, is not deductible.
6. Any amount paid for **brokerage or commission** for arrangement of the loan, is not deductible.
7. For the financial year in which construction of house property is completed, interest from 1st April till 31st March of that year, must be considered as previous year interest for that year. For example, if construction of house property is completed on 13th November, 2017, then construction being completed in previous year 2017-18, the interest for the entire financial year 2017-18 must be considered as previous year interest, and **not** interest from 13th November 2017 till 31st March 2018.
8. In practice, Housing Loans are repaid in installments, each installment consisting of both interest and principal component. The interest for any given period can be ascertained

from the 'Loan Repayment Schedule' given by the Bank or Institution from which the loan has been borrowed.

Illustration 6 Problem on Calculation of Interest deductible under section 24(b)

Mr. X borrowed a loan on 01-01-2011, of ₹2,50,000 @ 12% per annum, for construction of a house property. The construction of the property was completed on 15-08-2014. The following are the details of repayment of the *principal* amount:

On 01-07-2012	₹50,000
On 30-09-2013	₹60,000
On 01-03-2014	₹10,000
On 14-02-2017	₹80,000
On 31-10-2017	₹20,000
On 01-03-2018	₹20,000

Calculate deductions under section 24 for interest on borrowed capital for the previous year 2017-18.

Solution:

The situation given above is not realistic in nature. Re-payments of housing loan does not happen in this manner. They are paid in installments. However, this problem is created to understand the treatment for 'interest deductible under section 24(b)'.

	₹
Previous Year Interest (See Note No. 1)	4,800
Add: One-fifth of 'Pre-completion period interest' (See Note No. 2) (₹83,400 × 1/5)	16,680
Interest deductible under section 24(b)	21,480

Notes:

1. The relevant previous year is 2017-18. By the time of commencement of relevant previous year, out of ₹2,50,000 loan borrowed, assessee has repaid principal amount to the extent of ₹2,00,000. So, at the beginning of the relevant previous year, the loan amount outstanding is ₹50,000. During 2017-18, there are two re-payments made by the assessee (₹20,000 on 31st October 2017 and ₹20,000 on 1st March 2018).

So, the loan amount **outstanding** during previous year 2017-18 is—

₹50,000 for 7 months (from April 2017 to October 2017).

₹30,000 for 4 months (from November 2017 to February 2018).

₹10,000 for 1 month (for the month of March 2018).

Accordingly, the interest for previous year 2017-18 is—

$$(\text{₹}50,000 \times 12/100 \times 7/12) + (\text{₹}30,000 \times 12/100 \times 4/12) + (\text{₹}10,000 \times 12/100 \times 1/12) = \text{₹}4,800.$$

2. The loan was borrowed on 1st January 2011 and the Construction of the property was completed on 15th August 2014. So, the pre-completion period is 1st January 2011 till 31st March 2014 (39 months). Since, the loan has not yet been completely repaid, earlier of two options for ending date is not applicable.

During the above period of 39 months, two re-payments are made by the assessee (₹50,000 on 1st July 2012 and ₹60,000 on 30th September 2013)

So, the loan amount outstanding during 'pre-completion period' is—

₹2,50,000 for 18 months (from January 2011 to June 2012).

₹2,00,000 for 15 months (from July 2012 to September 2013)

₹1,40,000 for 6 months (from October 2013 to March 2014)

Accordingly, 'pre-completion period interest' is—

$$(\text{₹}2,50,000 \times 12/100 \times 18/12) + (\text{₹}2,00,000 \times 12/100 \times 15/12) + (\text{₹}1,40,000 \times 12/100 \times 6/12) = \text{₹}83,400$$

3. The construction being completed during previous year 2014-15, the deduction for 'pre-completion period interest' is available for previous years 2014-15, 2015-16, 2016-17, 2017-18 and 2018-19. Since, the relevant previous year of the assessee (2017-18) is one among the above five years, deduction for pre-construction period must be considered.

After providing for deductions under section 24 from Net Annual Value, the balance may be **positive or negative**. The positive balance represents 'Income from House Property' and the negative balance represents 'Loss from House Property'.

Illustration 7 Problem on computing taxable income from let-out property

Compute taxable income from house property from the following particulars:

	₹
Fair Rental Value	80,000
Actual Rent	72,000
Municipal Valuation	50,000
Standard Rent	60,000
Municipal Taxes	20%
Interest paid	18,000

Solution:

Though the problem does not specify, the property is a let-out property since 'Actual Rent' is given.

Computation of Income from House Property

	₹	₹
Gross Annual Value (See Note No. 1)		72,000
Less: Municipal Taxes <i>paid</i> by the <i>assessee</i> during the <i>previous year</i> . (20% of Municipal Value – 20% of ₹ 50,000)		10,000
Net Annual Value		62,000
Less: Deductions under section 24		
Standard Deduction (30% of Net Annual Value)	18,600	
Interest on borrowed capital (given)	18,000	36,600
Income from House Property		25,400

Notes:

1. Calculation of Gross Annual Value

	₹
Step One – Calculation of Notional Rent (Higher of Municipal Value and Fair Rental Value, restricted to Standard Rent)	60,000
Step Two – Calculation of Rent Recovered (Annual Rent <i>less</i> Unrealised Rent)	72,000
Step Three – Calculation of Gross Annual Value (Higher of Steps 1 and 2 <i>minus</i> Vacancy period rent)	72,000

Note: There is no information about ‘unrealised rent’ and ‘vacancy period rent’.

2. When Municipal Taxes are given as a percentage, it must be calculated on Municipal Value.

Illustration 8 Problem on computing taxable income from let-out property, when NAV is negative

Compute income from house property from the following information:

	₹
Actual Rent	90,000
Municipal Taxes paid by Owner during previous year	
Of 2017-18	30,000
Of earlier years	70,000
Repair expenses	6,000
Interest on loan borrowed for purchase of property	25,000

Solution:**Computation of Income from House Property**

	₹	₹
Gross Annual Value (Actual rent itself)		90,00
Less: Municipal Taxes <i>paid</i> by the <i>assessee</i> during the <i>previous year</i> .		1,00,000
Net Annual Value		(-)10,000
Less: Deductions under section 24		
(a) Standard Deduction (30% of Net Annual Value)	Nil	
(b) Interest on borrowed capital (given)	25,000	25,000
Income from House Property		(-)35,000

Illustration 9 Problem on computing taxable income from let-out property

Shri Ramesh Kumar is owner of three houses:

Particulars	House A	House B	House C
Annual fair rent	18,000	15,000	12,000
Municipal valuation	15,000	20,000	10,000
Rent per month	2,000	1,500	1,250
Use by tenant	Residential	Office	Residential
Construction started	30.05.2010	01.01.2012	02.03.2009
Construction completed	01.04.2014	01.06.2016	31.03.2012
Repair expenses	1,000	—	4,000
Collection charges	2,000	500	—
Interest on loan:			
(a) For construction.	10,000	—	—
(b) For marriage of daughter	—	6,000	—
(c) For repair	—	—	1,000

Municipal tax is 10% of municipal valuation. Municipal tax of House A was paid by owner but Municipal tax of House B was not paid up to 31st March, 2018. Municipal tax of house C was paid by the tenant. House C was vacant for four months during the previous year 2017-18. Compute income from house property for the assessment year 2018-19.

(Bangalore University, B.Com, December 2014 and December 2016 (Modified))

Solution:

**Computation of Taxable Income from House Property of Mr. Ramesh Kumar for
Assessment Year 2018-19**

	House A	House B	House C
Gross Annual Value (See Note No. 1)	24,000	20,000	10,000
Less: Municipal Taxes <i>Paid</i> by the <i>assessee</i> during the <i>previous year</i> (See Note No. 2)	1,500	Nil	Nil
Net Annual Value	22,500	20,000	10,000
Less: Deductions under section 24			
(a) Standard Deduction (30% of Net Annual Value)	(-) 6,750	(-) 6,000	(-) 3,000
(b) Interest on borrowed capital (See Note No. 3)	(-) 10,000	Nil	(-) 1,000
Income from House Property	5,750	14,000	6,000

Total Taxable Income from House Property = ₹25,750 (i.e., ₹5,750 + ₹14,000 + ₹6,000)

Notes:

1. Calculation of Gross Annual Value

	House A ₹	House B ₹	House C ₹
Step One – Calculation of Notional Rent (Higher of Municipal Value and Fair Rental Value, restricted to Standard Rent)	18,000	20,000	12,000
Step Two – Calculation of Rent Recovered (Annual Rent <i>less</i> Unrealised Rent)	24,000	18,000	15,000
Step Three – Calculation of Gross Annual Value (Higher of Steps 1 and 2 <i>minus</i> Vacancy period rent)	24,000	20,000	15,000 – (4 × 1250) = 10,000

2. Municipal Taxes

Municipal Taxes are 10% of Municipal Value. Accordingly, for the municipal taxes for each House are:

House A – ₹1,500

House B – ₹2,000

House C – ₹1,000.

It is deductible only for House A since - for House B it is not yet paid; and for House C it is paid by the tenant.

3. Interest on loan borrowed is not deducted for House B since the loan is not borrowed for property purposes.

Illustration 10 Problem on computing taxable income from let-out property

Mr. X is the owner of a house property, the construction of which was completed on 11-09-2013. The property has 4 units – 3 residential and one commercial. The municipal value of the property is ₹2,50,000 and the rent of a similar accommodation in the same locality is ₹21,000 per month. However, the standard rent as per Rent Control Act is ₹20,500 per month, for the entire property. Each residential unit has been let out for a rent of ₹5,000 per month, while the commercial unit has been let out @ ₹6,000 per month.

During March 2018, the entire property was vacant and there was 2 months unrealized rent from the commercial unit and 6 months unrealized rent from one of the residential units. All conditions for deduction of unrealized rent have been satisfied.

The municipal authorities levied tax @ 10% on the property, 60% of which was paid by X and the balance by the tenants. The assessee incurred repair expenditure on the property of ₹40,000 during the financial year 2017-18 and rent collection charges of ₹500. Further, he paid land revenue of ₹6,000 on the property for the year.

For construction of the property, X had borrowed ₹10,00,000 on 01-04-2011 @ 10% per annum. The following are the details of repayment of the principal amount:

On 01-04-2012	₹2,00,000.
On 01-04-2013	₹2,00,000
On 01-08-2016	₹2,00,000
On 01-01-2017	₹2,00,000
On 31-10-2017	₹2,00,000

Compute the taxable income from house property for the assessment year 2018-19.

Solution:

Computation of Income from House Property

	₹	₹
Gross Annual Value (See Note No. 1)		2,25,000
Less: Municipal Taxes <i>paid</i> by the <i>assessee</i> during the <i>previous year</i> . [₹2,50,000 × 10/100 × 60/100] – (See Note No. 2)		15,000
Net Annual Value		2,10,000
Less: Deductions under section 24		
(a) Standard Deduction (30% of Net Annual Value)	63,000	
(b) Interest on borrowed capital (See Note No. 3)	47,667	1,10,667
Income from House Property		99,333

Notes:1. Calculation of Gross Annual Value

	₹
Step One – Calculation of Notional Rent Municipal Value (₹2,50,000) or Fair Rental Value (₹21,000 × 12 = ₹2,52,000), whichever is higher = ₹2,52,000 Or Standard Rent (₹20,500 × 12) = ₹2,46,000 Whichever is lower	2,46,000
Step Two – Calculation of Rent Recovered Actual Rent per annum [(₹5,000 × 12 × 3) + (₹6,000 × 12 × 1)] = ₹2,52,000 Less: Unrealised Rent [(₹6,000 × 2) + (₹5,000 × 6)] = ₹42,000	2,10,000
Step Three – Calculation of Gross Annual Value Higher of steps 1 and 2 ₹2,46,000 Less: Vacancy period rent [(₹5,000 × 3) + ₹6,000] ₹21,000	2,25,000

2. Municipal Taxes are calculated on municipal value. Municipal taxes paid by tenant are not deductible. Hence, only the extent of municipal taxes paid by owner (60%) is deducted.

3. Interest on Borrowed Capital:

	₹
Previous Year Interest (See Point (a) below)	11,667
Add: One-fifth of 'Pre-completion period interest' (See Point (b) below) (₹1,80,000 × 1/5)	36,000
Interest deductible under section 24(b)	47,667

Explanation

(a) The relevant previous year is 2017-18. By the time of commencement of relevant previous year, out of ₹10,00,000 loan borrowed, assessee has repaid principal amount to the extent of ₹8,00,000. So, at the beginning of the relevant previous year, the loan amount outstanding is ₹2,00,000. During 2017-18, there is a re-payment of ₹2,00,000 made on 31st October 2017.

So, the loan amount outstanding during previous year 2017-18 is–

₹2,00,000 for 7 months (from April 2017 to October 2017).

Accordingly, the interest for previous year 2017-18 is–

(₹2,00,000 × 10/100 × 7/12) = **₹11,667.**

(b) The loan was borrowed on 1st April 2011, the construction of the property was completed on 11th September 2013 and the entire loan amount has been repaid on 31st October 2017.

The starting date of pre-completion period is 1st April 2011.

The ending date of pre-completion period is *earlier* of 31st March preceding the date of completion of construction (i.e., 31st March 2013) or date on which loan has been completely repaid (i.e., 31st October 2017). The earlier of the two is 31st March 2013.

So, the 'pre-completion period' is 1st April 2011 to 31st March 2013 (24 months)

During the above period of 24 months, one re-payment of ₹2,00,000 has been made on 1st April 2012.

So, the loan amount outstanding during 'pre-completion period' is—

₹10,00,000 for 12 months (from April 2011 to March 2012)

₹8,00,000 for 12 months (from April 2012 to March 2013)

Accordingly, 'pre-completion period interest' is—

$(₹10,00,000 \times 10/100 \times 12/12) + (₹8,00,000 \times 10/100 \times 12/12) = ₹1,80,000$

- (c) The construction being completed during previous year 2013-14, the deduction for 'pre-completion period interest' is available for previous years 2013-14, 2014-15, 2015-16, 2016-17 and 2017-18. Since, the relevant previous year of the assessee (2017-18) is one among the above five years, deduction for pre-construction period must be considered.

Composite Rent

Where the assessee, being owner of a property, has let out the property along with certain amenities or facilities like free supply of water, electricity, gas, free maintenance of the property, garden, swimming pool, staircase, etc., then, the rent charged for the property will be called as 'Composite Rent'.

When the rental agreement specifies clearly the rent for the property and the charge for amenities, then the rent will be considered as 'actual rent'; and the charges for amenities will be taxable to the extent the charges exceed the cost of providing such amenities. The excess amount will be taxable under the head 'Income from Business' (if assessee is engaged in the business of letting out properties) or 'Income from other sources'.

For example, suppose assessee charges ₹15,000 as rent per month, of which ₹2,500 is for facilities. Then, the actual rent will be taken as ₹12,500 per month, in computation of Gross Annual Value. Suppose, the actual electricity, water and other bills paid by assessee are ₹2,000 per month. Then, the excess amount of ₹6000 $[(₹2,500 - ₹2,000) \times 12]$ will be taxable under the relevant head.

However, where the rental agreement does not specify the amount charged towards facilities/services, then the actual expenditure incurred by the assessee to provide facilities will be considered as amount recovered from tenant for the facilities and only the balance amount of rent will be considered as 'Actual Rent' in computation of Gross Annual Value.

For example, suppose the rent charged for a property is ₹15,000 per month. The assessee has provided free electricity and water supply, the bills for which amount to ₹30,000 for the relevant previous year. Assuming that, out of rent charged ₹30,000 is collected towards service, the balance amount of ₹1,20,000 [i.e., $(₹15,000 \times 12) - ₹30,000$] will be considered as 'Actual Rent'.

Illustration 11 Problem on computing taxable income from let-out property, when there is composite-rent

Mr. Kiran is the owner of a house property. Its municipal valuation is ₹6,00,000. It has been let out for ₹9,00,000 per annum. The local taxes payable by the owner amount to ₹1,00,000 but as per agreement between tenant and landlord, the tenant had paid them directly to the municipality. The landlord however, incurs the following expenses on the tenant's amenities during the year 2017-18:

Water charges – ₹10,000

Lift maintenance – ₹10,000

Salary of gardener – ₹12,000

Lighting of stairs – ₹8,000

Maintenance of swimming pool – ₹5,000

Expenses of water connection – ₹20,000

The landlord claims the following deductions:

Repairs – ₹3,00,000

Land revenue paid – ₹10,000

Collection charges – ₹20,000

Compute taxable income from house property for the assessment year 2018-19.

Solution:
Computation of Income from House Property of Mr. Kiran for Assessment Year 2018-19

	₹	₹
Gross Annual Value (See Note No. 1)		8,55,000
Less: Municipal Taxes <i>paid</i> by the <i>assessee</i> during the <i>previous year</i> . (not deductible, since it has been paid by tenant)		Nil
Net Annual Value		8,55,000
Less: Deductions under section 24		
Standard Deduction (30% of Net Annual Value)	2,56,500	
Interest on borrowed capital (not given)	NA	2,56,500
Income from House Property		5,98,500

Notes:
1. Calculation of Gross Annual Value

	₹
Step One – Calculation of Notional Rent	
Only Municipal Value available	6,00,000

	₹
Step Two – Calculation of Rent Recovered	
<i>Actual Rent per annum</i>	
Rent charged	9,00,000
<i>Less: Amount recovered for services</i> (assumed to have recovered the actual expenditure)	
Water charges	10,000
Lift Maintenance	10,000
Salary of Gardener	12,000
Lighting of Stairs	8,000
Maintenance of Swimming Pool	5,000
Water connection (does not amount to amenity)	----- 45,000
Step Three – Calculation of Gross Annual Value	8,55,000
Higher of steps 1 and 2	

2. Water connection is a basic facility to be made available to the residents of a property. Expenses which tenant must have incurred, when incurred by assessee becomes amenity or benefit provided to tenant.

10.3.2 Self Occupied Property

When a property owned by the assessee is used by him for his own residential occupation, it is called 'self-occupied property'. Where the property is used by the assessee for his business or profession, such property will be considered under the head "Business and Profession". However, where the property owned by the assessee is meant for residential occupation, it is chargeable under the head "Income from House Property".

The property might be used by the assessee himself, or his parents, or his children or the HUF in which assessee is a member. In any of these cases, the property will be regarded as 'self-occupied property'. Any property kept vacant by the assessee for the entire period of relevant previous year will also be regarded as 'Self-occupied property'.

The following is the format for computing 'income from self-occupied property':

	₹	₹
Annual Value		Nil
Less Deduction under section 24(b) – Interest on borrowed capital		XXX
Income from House Property		XXX

Notes:

1. Since, the assessee does not get any monetary benefit from the property, the Annual Value for a self-occupied property is 'Nil' in accordance with section 23(2)(a) and 23(2)(b).

2. The 'Annual Value' in the above case refers to the **value after deduction for payment** of municipal taxes.
3. A self-occupied property is eligible for only one deduction under section 24(b) – towards Interest on borrowed capital.
4. The deduction under section 24(b) for a self-occupied property must be calculated as under–
 Amount of interest as per format
 Or
 Maximum Limit
 Whichever is less.
5. The interest as per format is the amount of interest calculated as explained earlier. It is calculated using the following format:

	₹
Previous Year Interest	XXX
Add: One-fifth of 'Pre-completion period interest'	XXX
	XXX

6. Maximum Limit for deduction under section 24(b) in case of self-occupied property
 - When **all** of the three prescribed conditions are fulfilled – ₹2,00,000.
 - Otherwise – ₹30,000
7. Conditions for considering ₹2,00,000 as Maximum Limit
 - (a) The loan must have been borrowed **on or after** 1st April, 1999.
 - (b) The loan must be borrowed for **purchase or construction** of house property or for re-payment of an earlier loan which had been borrowed for **purchase or construction** of house property. The old loan might have been borrowed even prior to 1st April, 1999.
 - (c) The purchase or construction of property must be completed **within five years from the last date of the financial year** during which the loan (i.e., original loan) was borrowed.
8. The second condition above states that the loan must be borrowed for purchase or construction of property. Where the loan is borrowed for any other purpose of property like repairs, alterations, renewals, reconstruction, etc., the second condition is not said to be fulfilled.
9. The third condition specifies the period by which the purchase or construction of property must be completed. Suppose, assessee borrowed loan for purchase or construction of property in July 2016. In this case, the loan has been borrowed during financial year 2016-17. The last date of this financial year is 31st March 2017. So, the purchase or construction must be completed within five years from 31st March 2017, i.e., by 31st March 2022.
10. In case the present loan was borrowed to repay an earlier housing loan, the third condition must be applied for the original loan.

11. Only when **all the conditions** are fulfilled, the maximum limit can be taken as ₹2,00,000. When **any or all of the above conditions are not fulfilled**, the maximum limit must be taken as ₹30,000.
12. The maximum limit for deduction under section 24(b) is applicable **only** for properties which are assessed as 'self-occupied properties'.
13. Where an assessee owns a house property, but is not in its occupation on account of his **employment, business or profession carried on at any other place**, and has to reside at such other place in a house property not belonging to him, then the property owned by the assessee, though not occupied must be assessed as self-occupied property.
14. If the assessee let out his house to his employer, which in turn allots the same to him, as rent free accommodation, such house will **not** be treated as self-occupied, because he is not occupying his own house in the capacity of owner.

Illustration 12 Problem on deciding the maximum limit for deduction under section 24(b) in case of a self-occupied property

Specify the maximum limit for deduction under section 24(b) in case of loan borrowed by Mr. X towards his self-occupied property.

Sl. No.	Situation
1.	X has borrowed the loan on 1.8.1998 for purchase of house property
2.	X has borrowed the loan on 1.1.2014 for purchase of house property
3.	X has borrowed the loan on 1.11.2011 for repairs of house property
4.	X has borrowed the loan on 1.7.2010 for repayment of an earlier loan borrowed in May 1997 for construction of house property
5.	X had borrowed loan in June 2012 for construction of house property and the construction of property was completed during September 2014
6.	X had borrowed loan in August 2016 for construction of house property and the construction of property was completed during May 2022
7.	X had borrowed a loan in October 2013 for repayment of an earlier loan which was borrowed in June 1996 for construction of house property. The construction of the property was completed in December 2003.

Solution:

Sl. No.	Situation	Maximum Limit for deduction under section 24(b)
1.	X has borrowed the loan on 1.8.1998 for purchase of house property	₹30,000
2.	X has borrowed the loan on 1.1.2014 for purchase of house property	₹2,00,000

Sl. No.	Situation	Maximum Limit for deduction under section 24(b)
3.	X has borrowed the loan on 1.11.2011 for repairs of house property	₹30,000
4.	X has borrowed the loan on 1.7.2010 for repayment of an earlier loan borrowed in May 1997 for construction of house property	₹2,00,000
5.	X had borrowed loan in June 2012 for construction of house property and the construction of property was completed during September 2014	₹2,00,000
6.	X had borrowed loan in August 2016 for construction of house property and the construction of property was completed during May 2022	₹30,000 (Since the construction of property is completed after 5 years from the last date of the year during which the loan was borrowed – i.e., after 5 years from 31.03.2017)
7.	X had borrowed a loan in October 2013 for repayment of an earlier loan which was borrowed in June 1996 for construction of house property. The Construction of the property was completed in December 2003.	₹2,00,000

Illustration 13 Problem on computing income from self-occupied property

Yoganand has a house property in Navi Mumbai. He stays with his family in this house. The rent of a similar accommodation in the same locality is ₹6,00,000 per annum. The municipal value of the property is ₹5,00,000. Municipal taxes paid during previous year 2017-18 was ₹48,000 (including ₹10,000 of earlier years). The house was constructed in 1998 with a loan of ₹12,00,000 borrowed from LIC Housing Finance Ltd. During the previous year 2017-18, Yoganand refunded ₹4,36,000 of which ₹1,39,000 was interest component. Compute the taxable income from house property for the assessment year 2018-19.

What would be the income from house property if the loan was borrowed in June 2009 and the construction of the property was completed in May 2011?

Solution:

The computation of taxable income is shown under two situations—

Situation (1) – When the construction of the property was completed in 1998, out of loan borrowed before that date.

Situation (2) – When the construction of the property was completed in 2011, out of loan borrowed in 2009.

Computation of Income from House Property of Yoganand for Assessment Year 2018-19

	Situation (1) ₹	Situation (2) ₹
Gross Annual Value	Nil	Nil
Less: Deduction under section 24(b) – Interest on borrowed capital (See Note below)	30,000	1,39,000
Income from House Property	(–) 30,000	(–)1,39,000

Note:

The deduction under section 24(b) is calculated as follows–

	Situation (1) ₹	Situation (2) ₹
Interest as per format		
Previous year Interest (given)	1,39,000	1,39,000
Pre-completion period interest (not applicable since Previous year 2017-18 is not among the first five years)	Nil	Nil
	1,39,000	1,39,000
OR		
Maximum Limit (considered since the property is self-occupied property)	30,000	2,00,000
Whichever is Less	30,000	1,39,000

10.3.3 Deemed to be Let Out Property

Where the assessee is in occupation of more than one residential property owned by him (i.e., when assessee has more than one self-occupied property), then for tax purposes, only one of the self-occupied properties must be assessed as ‘self-occupied property’ and the other self-occupied properties must be treated as let-out properties and assessed accordingly. The self-occupied properties which are treated as let-out properties for assessment purposes are called ‘Deemed to be let-out Properties’.

For assessment purposes, among the different self-occupied properties, the assessee can opt for the property which he wants to be assessed as self-occupied property. In case, assessee has not made any such option, the property to be assessed as self-occupied property must be identified based on the impact of tax (i.e., whichever property when assessed as ‘self-occupied property’ results in lowest taxable income under this head, must be considered as self-occupied property, and the other self-occupied properties must be assessed as ‘deemed to be let out properties’).

The following is the format for computing income from a ‘deemed to be let-out property’:

10.30 • Income Tax - I

	₹	₹
Gross Annual Value (See Note 1 below)		XXX
Less: Municipal Taxes <i>paid</i> by the <i>assessee</i> during the <i>previous year</i> .		XXX
Net Annual Value		XXX
Less: Deductions under section 24		
Standard Deduction	XXX	
Interest on Borrowed Capital	XXX	XXX
		XXX

Notes:

1. Since the property is not actually let-out, but treated as let-out, there is no actual rent for the property. Hence, Notional Rent or Expected Rent itself is the Gross Annual Value for such property.
2. There is no maximum limit for deduction towards interest on borrowed capital. The maximum limit is applicable only when the property is assessed as self-occupied property.

Illustration 14 Problem on Computation of Income from self-occupied property and deemed to be let out properties

Mr. Mahesh has two flats in Chennai, one occupied by him and another occupied by his parents and children, the particulars of which are provided below:

	Flat I (occupied by Mr. Mahesh) ₹	Flat II (occupied by parents) ₹
Municipal valuation	24,000	42,000
Flat rent (rent which similar accommodation would fetch)	34,000	36,000
Standard rent	30,000	45,000
Municipal taxes paid	6,000	8,000
Repairs	12,000	4,000
Insurance premium	1,500	1,800
Interest on loan		
Loan availed on 01.04.2013	12,000	—
Loan availed on 01.04.2003	—	60,000

You are required to advise Mr. Mahesh which flat can be treated as self-occupied and the other deemed to be let out in a manner beneficial to him.

Solution:

Where the choice of the assessee is given or known, assessment can be made accordingly. However, in this case, assessee has not specified the property he prefers to be assessed as 'self-occupied property'. Hence, the following options are considered:

Option 1: To assess Flat I as Self-occupied property and Flat II as 'Deemed to be Let out'.

Option 2: To assess Flat II as Self-occupied property and Flat I as 'Deemed to be Let out'.

The taxable income from house properties, under both options, have been summarised in the following table:

Particulars	Option 1 (Flat I is Self-occupied Property) ₹	Option 2 (Flat II is Self-occupied property) ₹
Income from Flat I (See Working Note)	(–) 12,000	4,800
Income from Flat II (See Working Note)	(–) 36,200	(–) 60,000
Income from House Property	(–) 48,200	(–) 55,200

Since, the loss from House Property is high (i.e., taxable income is low) under Option 2, it is advisable for the assessee to assess Flat II as Self-occupied Property and Flat I as Deemed to be Let out Property.

Working Note:

	Flat I ₹	Flat II ₹
<i>When the property is assessed as self-occupied property</i>		
Annual Value	Nil	Nil
<i>Less: Deduction under section 24(b)</i>		
(Least of the interest amount or Maximum Limit – in both cases, the maximum limit is ₹2,00,000 assuming that the last condition is also fulfilled)		
	12,000	60,000
	(–) 12,000	(–) 60,000
<i>When the property is assessed as deemed to be let out property</i>		
Gross Annual Value (Higher of Municipal Value and Fair Rental Value, restricted to Standard Rent)	30,000	42,000
<i>Less: Municipal Taxes paid by the assessee during previous year</i>	6,000	8,000
Net Annual Value	24,000	34,000
<i>Less: Deductions under section 24</i>		
(a) Standard Deduction (30% of Net Annual Value)	(–) 7,200	(–) 10,200
(b) Interest on borrowed capital	(–) 12,000	(–) 60,000
	4,800	(–) 36,200

Illustration 15 **Problem on Computation of Income from self-occupied property and deemed to be let out properties**

Mr. X owns four houses which are used by him for his residential purposes:

	House One ₹	House Two ₹	House Three ₹	House Four ₹
Municipal Valuation	30,000	70,000	92,000	28,000
Fair Rent	40,000	58,000	96,000	37,000
Standard Rent	37,000	74,000	NA	36,000
Municipal Tax paid by X	3,000	16,000	29,000	12,000
Insurance premium	1,000	2,000	11,700	2,810
Interest on cap. borrowed to pay municipal tax	600	400	—	300
Interest on capital borrowed for construction (inclusive of one-fifth of pre-completion period's interest). In case of House Three capital is borrowed on April 10, 2009 and in other cases, before 1 st April, 1999.	11,060	75,900	54,090	85,300
Interest on capital borrowed for repairs of the property (interest is payable outside India and tax is not deducted at source)	—	—	5,020	12,600

Compute the taxable income from house property of Mr. X for the assessment year 2018-19.

Solution:

Where the choice of the assessee is given or known, assessment can be made accordingly. However, in this case, assessee has not specified the property he prefers to be assessed as 'self-occupied property'. Hence, the following options are considered:

Option 1: To assess House One as Self-occupied property and other properties as 'Deemed to be Let out'.

Option 2: To assess House Two as Self-occupied property and other properties as 'Deemed to be Let out'.

Option 3: To assess House Three as Self-occupied property and other properties as 'Deemed to be Let out'.

Option 4: To assess House Four as Self-occupied property and other properties as 'Deemed to be Let out'.

The taxable income from house properties, under all the above options, have been summarised in the following table:

Income from	Option 1 (House One is Self-occupied Property) ₹	Option 2 (House Two is Self-occupied Property) ₹	Option 3 (House Three is Self-occupied Property) ₹	Option 4 (House Four is Self-occupied Property) ₹
House One	(-) 11,060	12,740	12,740	12,740
House Two	(-) 38,100	(-) 30,000	(-) 38,100	(-) 38,100
House Three	(-) 7,190	(-) 7,190	(-) 54,090	(-) 7,190
House Four	(-) 68,500	(-) 68,500	(-) 68,500	(-) 30,000
Income from H P	(-) 1,24,850	(-) 92,950	(-) 1,47,950	(-) 62,550

Since, the loss from House Property is high (i.e., taxable income is low) under Option 3, it is advisable for the assessee to assess House Three as Self-occupied Property and House One, Two and Four as Deemed to be Let out Properties.

Working Note:

	House One ₹	House Two ₹	House Three ₹	House Four ₹
When the property is assessed as self-occupied property				
Annual Value	Nil	Nil	Nil	Nil
Less: Deduction under section 24(b) – Interest on borrowed capital (Amount of interest or maximum limit, whichever is less)	(-) 11,060	(-) 30,000	(-) 54,090	(-) 30,000
	(-) 11,060	(-) 30,000	(-) 54,090	(-) 30,000
When the property is assessed as deemed-to-be-let out property				
Gross Annual Value (Notional rent itself)	37,000	70,000	96,000	36,000
Less: Municipal Taxes <i>paid</i> by <i>assessee</i> during <i>previous year</i>	3,000	16,000	29,000	12,000
Net Annual Value	34,000	54,000	67,000	24,000
Less: Deductions under section 24				
(a) Standard Deduction (30% of NAV)	(-) 10,200	(-) 16,200	(-) 20,100	(-) 7,200
(b) Interest on borrowed capital	(-) 11,060	(-) 75,900	(-) 54,090	(-) 85,300
	12,740	(-) 38,100	(-) 7,190	(-) 68,500

Notes:

- Interest on loan borrowed to pay municipal taxes and interest paid outside India without deducting tax at source, are not deductible.

- When the properties are being assessed as self-occupied properties, the deduction for interest is restricted to maximum limit. Other than for House Three, in case of all other properties, the loan was borrowed before 1st April 1999. Hence, the maximum limit towards deduction of interest in case of House One, House Two and House Four are ₹ 30,000.
- In case of house Three, the loan has been borrowed after 1st April 1999. Assuming that the other two conditions are fulfilled, the maximum limit has been taken as ₹ 2,00,000.

10.3.4 Partly Let Out and Partly Self-Occupied Property

This type of property can be further classified into two categories, viz.,

- Portion Let out and Portion Self-occupied Property.
- Period Let out and Period Self-occupied Property.

The provisions for computing taxable income for each of the above categories are discussed below:

Portion Let out and Portion Self-occupied Property

Where one portion of the property is let-out and the remaining portion is self-occupied, then the income from such property must be computed in the following manner:

	₹
Income from let-out portion (using the format of let-out property)	XXX
Income from self-occupied portion (using the format of self-occupied property)	XXX
	XXX

While computing **income from let-out portion**, the following points must be kept in mind:

- The 'Gross Annual Value' must be taken as **higher** of 'Notional Rent **proportionate** to let-out portion' or '(Actual Rent p.a. for let out portion **less** unrealised rent)' **minus** vacancy period rent, if any.
- Municipal taxes and interest on borrowed capital **proportionate** to let-out portion of the property must only be deducted.

While computing **income from self-occupied portion**, the following point must be kept in mind:

- The 'Gross Annual value' for the self-occupied portion must be taken as Nil.
- Deduction for 'interest on borrowed capital' must be **least** of interest **proportionate** to self-occupied property or maximum limit.

Illustration 16

Problem on Computation of Income from portion let-out and portion self-occupied property

Mr. X owns one residential house in Mumbai. The house is having **two units of equal size**. First unit of the house is self-occupied by Mr. X and another unit is rented for ₹ 16,000 per month. The rented unit was vacant for 2 months during the year. The particulars of house for the previous year 2017-18 are as follows:

	₹
Standard rent	1,62,000 per annum
Municipal valuation	1,90,000 per annum
Fair rent	1,85,000 per annum
Municipal tax	15% of Municipal Valuation
Light and water charges	500 per month
Interest on borrowed capital	8,000 per month
Ground Rent	1,200 per annum
Insurance charges	3,000 per annum
Repairs	12,000 per annum

Compute income from house property of Mr. X for the assessment year 2018-19.

Solution:

The property is a 'portion let-out (50%) and portion self-occupied property (50%)'. The taxable income for this property is calculated in the following manner:

	₹
Income from Unit 1 (Self-occupied) – See Working Note Below.	(–) 48,000
Income from Unit 2 (Let-out) – See Working Note below.	54,025
Income from House Property	6,025

Working Notes:

Income from Unit 1 (Self-occupied portion)

	₹	₹
Annual Value		Nil
Less: Deduction under section 24(b) – Interest on borrowed capital		
Interest amount proportionate to self-occupied portion (₹8,000 × 12 × 50/100)	48,000	
OR		
Maximum Limit (assuming all conditions for higher maximum limit are fulfilled)	2,00,000	
Whichever is less		48,000
		(–) 48,000

Income from Unit 2 (Let-out Portion)

	₹	₹
Gross Annual Value (See Note below)		1,60,000
Less: Municipal Taxes <i>paid</i> by the <i>assessee</i> during the <i>previous year</i> – in proportion to let-out portion ($15/100 \times ₹1,90,000 \times 50/100$)		14,250
Net Annual Value		1,45,750
Less: Deductions under section 24		
Standard Deduction (30% of Net Annual Value)	43,725	
Interest on borrowed capital proportionate to let-out portion ($₹8,000 \times 12 \times 50/100$)	48,000	91,725
Income from Let-out Portion		54,025

Notes:**Calculation of Gross Annual Value**

	₹
Step One – Calculation of Notional Rent	
Municipal Value (₹1,90,000) or Fair Rental Value (₹1,85,000), whichever is higher = ₹1,90,000	
Or	
Standard Rent (₹1,62,000)	81,000
Whichever is lower - ₹1,62,000	
Notional Rent proportionate to let-out portion ($50/100 \times ₹1,62,000$)	
Step Two – Calculation of Rent Recovered	
Actual Rent per annum ($₹16,000 \times 12$)	₹1,92,000
Less: Unrealised Rent	Nil
Step Three – Calculation of Gross Annual Value	
Higher of steps 1 and 2	₹1,92,000
Less: Vacancy period rent ($₹16,000 \times 2$)	32,000

Illustration 17 **Problem on Computation of Income from portion let-out and portion self-occupied property**

Mr. Krishna owns a residential house in Delhi. The house is having two **identical units**. First unit of the house is self-occupied by Mr. Krishna and another unit is rented for ₹12,000 p.m. the rented unit was vacant for three months during the year. The particulars of the house for the previous year 2017-18 are as under:

Standard Rent	₹2,20,000 p.a.
Municipal Valuation	₹2,44,000 p.a.
Fair Rent	₹2,35,000 p.a.

Municipal tax paid by Mr. Krishna	12% of the Municipal Valuation
Light and water charges	₹ 800 p.m.
Interest on borrowed capital	₹ 2,000 p.m.
Insurance charges	₹ 3,500 p.a.
Painting expenses	₹ 16,000 p.a.

Compute income from house property of Mr. Krishna for the assessment year 2018-19.

Solution:

The property is a 'portion let-out and portion self-occupied property'. The taxable income for this property is calculated in the following manner:

	₹
Income from Unit 1 (Self-occupied) – See Working Note Below.	(–) 12,000
Income from Unit 2 (Let-out) – See Working Note below.	53,352
Income from House Property	41,352

Working Notes:

Income from Unit 1 (Self-occupied portion)

	₹	₹
Annual Value		Nil
Less: Deduction under section 24(b) – Interest on borrowed capital		
Interest amount proportionate to self-occupied portion (₹ 2,000 × 12 × 50/100)	12,000	
OR		
Maximum Limit (assuming all conditions for higher maximum limit are fulfilled)	2,00,000	
Whichever is less		12,000
		(–) 12,000

Income from Unit 2 (Let-out Portion)

	₹	₹
Gross Annual Value (See Note below)		1,08,000
Less: Municipal Taxes paid by the assessee during the previous year – in proportion to let-out portion (12/100 × ₹ 2,44,000 × 50/100)		14,640
Net Annual Value		93,360
Less: Deductions under section 24		
(c) Standard Deduction (30% of Net Annual Value)	28,008	
(d) Interest on borrowed capital proportionate to let-out portion (₹ 2,000 × 12 × 50/100)	12,000	40,008
Income from Let-out Portion		53,352

Notes:*Calculation of Gross Annual Value*

	₹
Step One – Calculation of Notional Rent Municipal Value (₹2,44,000) or Fair Rental Value (₹2,35,000), whichever is higher = ₹2,44,000 Or Standard Rent (₹2,20,000) Whichever is lower – ₹2,20,000 Notional Rent proportionate to let-out portion ($50/100 \times ₹2,20,000$)	1,10,000
Step Two – Calculation of Rent Recovered Actual Rent per annum ($₹12,000 \times 12$) ₹1,44,000 Less: Unrealised Rent Nil	1,44,000
Step Three – Calculation of Gross Annual Value Higher of steps 1 and 2 ₹1,44,000 Less: Vacancy period rent ($₹12,000 \times 3$) 36,000	1,08,000

Period Let Out and Period Self-occupied Property

Where the property was let-out by the assessee for some period during the relevant previous year and self-occupied for the remaining period of the relevant previous year, the property must be assessed as if it is a ***completely let-out property***.

However, while computing income from such property the actual rent per annum must be taken only for the let-out period and not for the whole previous year. The other provisions and deductions remain same as in case of a let-out property.

Illustration 18	Problem on Computation of Income from portion let-out and portion self-occupied property
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Ram owned a property at Chennai which was occupied by him for the purpose of his residence. He was transferred to Mumbai in June 2015 and therefore he let-out the property with effect from 1st July 2017 on a monthly rent of ₹30,000. The Fair rental value of the property was ₹2,40,000, whereas the Municipal Value of the property was ₹2,50,000.

The corporation tax payable in respect of the property was ₹35,000 of which 50 per cent was paid by him before 31.03.2018. Interest on money borrowed for the construction of the property amounted to ₹1,20,000. Compute the income from house property for the assessment year 2018-19.

Solution:**Computation of Income from House Property**

	₹	₹
Gross Annual Value (See Working Note below)		3,00,000
Less: Municipal Taxes <i>paid</i> by the <i>assessee</i> during the <i>previous year</i> (₹35,000 × 50/100)		17,500
Net Annual Value		2,82,500
Less: Deductions under section 24		
Standard Deduction (30% of Net Annual Value)	84,750	
Interest on borrowed capital proportionate to let-out portion	1,20,000	2,04,750
Income from House Property		77,750

Working Note:

	₹
Step One – Calculation of Notional Rent	
Municipal Value (₹2,50,000) or Fair Rental Value (₹2,40,000), whichever is higher = ₹2,50,000	2,50,000
Or	
Standard Rent (not given, assumed as Not applicable)	
Step Two – Calculation of Rent Recovered	
Actual Rent per annum (₹30,000 × 10)	₹3,00,000
Less: Unrealised Rent	Nil
Note: Since the property is portion let out and portion self-occupied, the actual rent per annum must not be taken for full year, but only for let-out period.	
Step Three – Calculation of Gross Annual Value	
Higher of steps 1 and 2	₹3,00,000
Less: Vacancy period rent	—

SPECIAL PROVISIONS UNDER THE HEAD 'INCOME FROM HOUSE PROPERTY'

10.4

The following are the other items or situations for which certain specific treatment is provided for under the Income Tax Act.

1. Recovery of unrealised rent and Arrears of rent received.
2. Co-ownership.
3. Property in foreign country.

10.4.1 Recovery of Unrealised Rent and Arrears of Rent Received [Section 25A]

When the owner of a property is not able to recover rent from tenant despite all his efforts, the amount of unrealised rent will be deducted while computing income from a let-out property. However, when such unrealised rent is later realised, it is taxable, irrespective of *whether the assessee is the owner of the property or not during the previous year in which unrealised rent is recovered*:

‘Arrears of rent received’ refers to additional rent of earlier previous years (i.e., years preceding the relevant previous year) received during the relevant previous year on account of increase in rent from retrospective effect.

Suppose, X had let out a property to Y for a monthly rent of ₹10,000. In July 2017, X increases the rent to ₹13,000 per month effective from April 2016. From April 2016 to June 2017, the number of months is 15. Suppose the tenant pays the additional rent of ₹3,000 per month for 15 months (i.e., ₹45,000) in July 2017. Out of ₹45,000 of additional rent received ₹36,000 pertains to the period preceding the previous year 2017-18. Such amount of additional rent of earlier period received during the relevant previous year, on account of increase in rent as effective from an earlier date, is called ‘Arrears of Rent’. Note in the above example, ₹36,000 of additional rent pertaining to the period preceding the relevant previous year is ‘arrears of rent’ and not ₹45,000.

The arrears of rent received is taxable in the year of receipt under the head ‘Income from House Property’, irrespective of *whether the assessee is still the owner of the house property or not*.

The taxable amount of ‘unrealised rent recovered’ and ‘arrears of rent received’ is calculated in the following manner:

	₹
Amount of Unrealised Rent Recovered and Arrears of Rent received	XXX
Less: Deduction under section 24(a) – Standard Deduction @ 30%	XXX
Taxable amount	XXX

Illustration 19 Problem on tax treatment for arrears of rent received u/s 25A

X owns a property. It is given on rent (rent being ₹27,500 per month) to a bank. Municipal value of the property is ₹3,25,000, fair rent ₹3,50,000 and standard rent ₹3,35,000. Municipal tax paid by X is as follows – ₹65,000 on January 10, 2017 and ₹75,000 on June 20, 2017. On August 1, 2017 rent is increased from ₹27,500 per month to ₹35,000 per month with retrospective effect from April 1, 2016. Arrears of rent of 2016-17 are paid in October 2017. Find out the income chargeable to tax for the assessment year 2017-18 and 2018-19.

Solution:

**Computation of Taxable Income from House Property for
Assessment Year 2017-18 (Previous year 2016-17)**

	₹	₹
Gross Annual Value (See Working Note No. 1 below)		3,35,000
Less: Municipal Taxes <i>paid</i> by the <i>assessee</i> during the <i>previous year</i>		65,000
Net Annual Value		2,70,000
Less: Deductions under section 24		
Standard Deduction (30% of Net Annual Value)	81,000	
Interest on borrowed capital	—	81,000
Income from House Property		1,89,000

**Computation of Taxable Income from House Property for
Assessment Year 2018-19 (Previous year 2017-18)**

	₹	₹
Gross Annual Value (See Working Note No. 2 below)		4,20,000
Less: Municipal Taxes <i>paid</i> by the <i>assessee</i> during the <i>previous year</i>		75,000
Net Annual Value		3,45,000
Less: Deductions under section 24		
Standard Deduction (30% of Net Annual Value)	1,03,500	
Interest on borrowed capital	—	1,03,500
		2,41,500
Add: Arrears of rent received under section 25A (See Working Note No.3 Below)		63,000
Income from House Property		3,04,500

Working Notes:

1. Computation of Gross Annual Value for Previous Year 2016-17 (Assessment Year 2017-18)

	₹
Step One – Calculation of Notional Rent	
Municipal Value (₹3,25,000) or Fair Rental Value (₹3,50,000), whichever is higher = ₹3,50,000	3,35,000
Or	
Standard Rent = ₹3,35,000	
Whichever is lower	

10.42 • Income Tax-I

		₹
Step Two – Calculation of Rent Recovered		
Actual Rent per annum ($₹27,500 \times 12$)	₹3,30,000	3,30,000
Less: Unrealised Rent	Nil	
Step Three – Calculation of Gross Annual Value		
Higher of steps 1 and 2	₹3,35,000	3,35,000
Less: Vacancy period rent	–	

2. Computation of Gross Annual Value for Previous Year 2017-18 (Assessment Year 2018-19)

In the absence of information, it is assumed that municipal value, fair rental value, standard rent and actual rent per annum remains the same for Previous Year 2017-18, as in Previous Year 2016-17.

		₹
Step One – Calculation of Notional Rent		
Municipal Value (₹3,25,000) or Fair Rental Value (₹3,50,000), whichever is higher = ₹3,50,000		3,35,000
Or		
Standard Rent = ₹3,35,000		
Whichever is lower		
Step Two – Calculation of Rent Recovered		
Actual Rent per annum ($₹35,000 \times 12$)	₹4,20,000	4,20,000
Less: Unrealised Rent	Nil	
Step Three – Calculation of Gross Annual Value		
Higher of steps 1 and 2	₹4,20,000	4,20,000
Less: Vacancy period rent	–	

3. Computation of Taxable Amount of Arrears of Rent Received u/s 25A

	₹
Amount of Arrears of Rent received (i.e., additional rent of the period preceding previous year 2017-18) – from April 2016 to March 2017 – $₹7,500 \times 12$	90,000
Less: Deduction under section 24(a) – $(30/100 \times ₹90,000)$	27,000
Taxable amount of Arrears of Rent Received	63,000

10.4.2 Property Owned by Co-owners [Section 26]

Where a house property is owned by more than one person, the share of each owner being *known or ascertainable*, there is said to be ‘**co-ownership**’.

The following is the tax provisions under section 26, for a co-owned property–

1. *Where the co-owned property is a let-out property or a property assessed as a ‘deemed to be let-out property’*

In case of such property, the income from the property must be computed presuming it is owned by a single owner. The taxable income (or loss) from such property must be distributed to each owner in the pre-determined ratio and such share must be included in the taxable income of each owner’s taxable income.

2. *Where the co-owned property is self-occupied by the owners*

In such case, the income from property must be calculated for each owner separately. Each owner must consider the Annual value as Nil and can claim deduction under section 24(b) for interest on borrowed capital. The amount of interest deductible by each owner will be ‘Proportionate share of interest on loan of the owner’ OR Maximum limit (₹30,000 or ₹2,00,000, whichever is applicable), whichever is less.

Note: Each owner can deduct their share of interest up to the maximum limit of either ₹30,000 or ₹2,00,000.

Illustration 20 Problem on co-owned property

The brothers Arun and Bimal are co-owners of a House Property with equal share. The property was constructed during the financial year 1999-2000. The property consists of eight identical units and is situated in Cochin.

During the financial year 2017-18, each co-owner occupied one unit for residence and the balance of six units were let out at a rent of ₹12,000 per month per unit. The municipal value of the house property is ₹9,00,000 and the municipal taxes are 20% of municipal value, which were paid during the year. The other expenses were as follows:

Repairs	₹40,000
Insurance premium (paid)	₹15,000
Interest payable on loan taken for construction of house	₹3,00,000

One of the let-out units remained vacant for four months during the year.

Arun could not occupy his unit for six months as he was transferred to Chennai. He does not own any other house.

The other income of Mr. Arun and Mr. Bimal are ₹2,90,000 and ₹1,80,000 respectively for the financial year 2017-18.

Compute the income under the head “Income from House Property” and the total income of two brothers for the assessment year 2018-19.

Solution:

The property is a 'portion let-out and portion self-occupied property'. Further, it is a case of co-ownership. The following is the tax treatment for this property:

1. Income from let-out portion of the property ($6/8 = 75\%$) must be calculated first and distributed to each owner in their agreed ratio (50% each).
2. Income from self-occupied portion must be calculated for each co-owner separately.

The taxable income of each co-owner is summarised in the table below:

	Arun ₹	Bimal ₹
Income from let-out portion – See Working Note No. 1	1,25,850	1,25,850
Income from self-occupied portion – See Working Note No. 2	(–) 37,500	(–) 37,500
Income from House Property	88,350	88,350
Add: Other Incomes	2,90,000	1,80,000
Total Income	3,78,350	2,68,350

Working Notes:

1. *Computation of Income from let-out portion of the property* $\left(\frac{6}{8}\right)$

	₹	₹
Gross Annual Value (See Note below)		8,16,000
Less: Municipal Taxes <i>paid</i> by the <i>assessee</i> during the <i>previous year</i> – in proportion to let-out portion $\left(₹9,00,000 \times 20/100 \times \frac{6}{8}\right)$		1,35,000
Net Annual Value		6,81,000
Less: Deductions under section 24		
Standard Deduction (30% of Net Annual Value)	2,04,300	
Interest on borrowed capital proportionate to let-out portion $(₹3,00,000 \times 6/8)$	2,25,000	4,29,300
Income from Let-out Portion		2,51,700

Each co-owner has equal share in the property. Hence, the share of taxable income from let out-portion for each owner is $₹2,51,700 \times \frac{1}{2} = ₹1,25,850$.

Note:Calculation of Gross Annual Value

	₹
Step One – Calculation of Notional Rent Municipal Value (₹9,00,000) or Fair Rental Value (not available), whichever is higher = ₹9,00,000 Or Standard Rent (not given – assumed rent control act is not applicable) Whichever is lower – ₹9,00,000 Notional Rent proportionate to let-out portion ($6/8 \times ₹9,00,000$)	6,75,000
Step Two – Calculation of Rent Recovered Actual Rent per annum ($₹12,000 \times 12 \times 6$) ₹8,64,000 Less: Unrealised Rent Nil	8,64,000
Step Three – Calculation of Gross Annual Value Higher of steps 1 and 2 ₹8,64,000 Less: Vacancy period rent ($₹12,000 \times 4$) 48,000	8,16,000

2. Computation of Income from Self-occupied Property for each co-owner

	Arun ₹	Bimal ₹
Annual Value	Nil	Nil
Less: Deduction under section 24(b) – Interest on borrowed capital		
Proportionate share of interest for each owner ($1/8 \times ₹3,00,000$)		
= ₹37,500		
OR		
Maximum Limit (assuming all prescribed conditions for higher maximum limit are fulfilled) = ₹2,00,000		
Whichever is less.	(–) 37,500	(–) 37,500
	(–) 37,500	(–) 37,500

Illustration 21 Problem on co-owned property

Mr. Raman is a co-owner of a house property along with his brother

	₹
Municipal value of the property	1,60,000
Fair rent	1,50,000
Standard rent under the Rent Control Act	1,70,000
Rent received	15,000 p.m.

The loan for the construction of this property is jointly taken and the interest charged by the bank is ₹25,000 out of which ₹21,000 have been paid. Interest on the unpaid interest is ₹450. To repay this loan, Raman and his brother have taken a fresh loan and interest charged on this loan is ₹5,000. The municipal taxes of ₹5,100 have been paid by the tenant. Compute the income from this property chargeable in the books of Mr. Raman for Assessment Year 2018-19.

Solution:

The property is co-owned. Being a let out property, the income from the property must be first computed and then the share of each owner must be shown under their respective taxable incomes.

**Computation of Taxable Income from House Property for
Assessment Year 2018-19 (Previous year 2017-18)**

	₹	₹
Gross Annual Value (See Working Note below)		1,80,000
Less: Municipal Taxes <i>paid</i> by the <i>assessee</i> during the <i>previous year</i>		Nil
Net Annual Value		1,80,000
Less: Deductions under section 24		
Standard Deduction (30% of Net Annual Value)	54,000	
Interest on borrowed capital proportionate to let-out portion (₹25,000 + ₹5,000)	30,000	84,000
Income from House Property		96,000

Working Note:

	₹
Step One – Calculation of Notional Rent	
Municipal Value (₹1,60,000) or Fair Rental Value (₹1,50,000), whichever is higher = ₹1,60,000	
Or	
Standard Rent = ₹1,70,000	
Whichever is lower	1,60,000
Step Two – Calculation of Rent Recovered	
Actual Rent per annum (₹15,000 × 12)	₹1,80,000
Less: Unrealised Rent	Nil
Step Three – Calculation of Gross Annual Value	
Higher of steps 1 and 2	₹1,80,000
Less: Vacancy period rent	–

Notes:

1. Municipal taxes have been paid by the tenant. Hence, it is not deductible.
2. Interest on borrowed capital is deductible on accrual basis. Hence, entire amount of ₹25,000 has been considered.

3. Interest on unpaid interest is not deductible.
4. Interest on new loan borrowed to repay and earlier housing loan is deductible. Hence, ₹5,000 has been considered for providing deduction u/s 24(b).
5. Since, the share of Mr. Raman is not known, the amount of income from this house property, taxable in his hands, cannot be ascertained.

10.4.3 House Property in a Foreign Country

Where assessee has a house property outside India, income from the property is taxable in the hands of the assessee based on residential status of the assessee:

- (a) Where the income from such property is received in India (first receipt), the income is taxable in the hands of the assessee, irrespective of his/her residential status.
- (b) Where the income from such property is received outside India, then the income is taxable in the hands of the assessee, only if the assessee is a 'resident and ordinarily a resident'.

The taxable income of a house property outside India must be computed in the same manner the income is calculated for a property in India. However, the income and expenses being in foreign currency, they must be translated into Indian currency (INR) and the computation must be made. For translation of foreign currency into Indian currency, the provisions explained in 'Accounting Standards' must be followed.

Illustration 22 Problem on computing income from property outside India

Mrs. Indu, a resident individual, owns a house in USA. She receives rent @ \$2000 per month. She paid municipal taxes of \$1500 during the financial year 2017-18. She also owns a two storied house in Mumbai, ground floor is used for her residence and first floor is let out at a monthly rent of ₹10,000. Standard rent for each floor is ₹11,000 per month. Municipal taxes paid for the house amounts to ₹7,500. Mrs. Indu had constructed the house by taking a loan from a nationalized bank on 20.06.2014. She repaid the loan of ₹54,000 including interest of ₹24,000. The value of one dollar is to be taken as ₹55.

Compute total income from house property of Mrs. Indu.

Solution:

The assessee has two properties – one in USA and one in Mumbai. The property in USA is let out and the property in Mumbai is 'partly let-out and partly self-occupied'.

The taxable income from house property of Ms. Indu is summarised in the following table:

	₹
Income from Property in USA (See Working Note No. 1)	8,66,250
Income from Property in Mumbai (See Working Note No. 2)	65,775
Income from House Property	9,32,025

Working Notes:**1. Computation of income from property in USA (let-out)**

	₹	₹
Gross Annual Value (only rent received is known and no other details required for calculating Gross Annual Value are available. Hence, the rent received itself is considered as Gross Annual value)		
(2,000\$ × ₹55 per \$ × 12 months)		13,20,000
Less: Municipal Taxes <i>paid</i> by the <i>assessee</i> during the <i>previous year</i>		
(1500\$ × ₹55 per \$)		82,500
Net Annual Value		<u>12,37,500</u>
Less: Deductions under section 24		
Standard Deduction (30% of Net Annual Value)	3,71,250	
Interest on borrowed capital proportionate to let-out portion	—	3,71,250
Income from House Property		<u>8,66,250</u>

2. Computation of income from Mumbai Property (portion let-out and portion self-occupied)

	₹
Income from ground floor (self-occupied) – See Working Note 3 below	(–) 12,000
Income from first floor (let-out) – See Working Note 4 below	77,775
	<u>65,775</u>

3. Computation of Income from self-occupied portion of Mumbai Property

	₹	₹
Annual Value		Nil
Less: Deduction under section 24(b) – Interest on borrowed capital		
Interest amount proportionate to self-occupied portion		
(₹24,000 × 50/100)	12,000	
OR		
Maximum Limit (assuming all conditions for higher maximum limit are fulfilled)	2,00,000	
Whichever is less.		(–) 12,000
		<u>(–)12,000</u>

4. *Computation of income from let-out portion of Mumbai Property*

	₹	₹
Gross Annual Value (See Working Note No. 5 below)		1,32,000
Less: Municipal Taxes <i>paid</i> by the <i>assessee</i> during the <i>previous year</i> – in proportion to let-out portion ($₹7,500 \times 50/100$)		3,750
Net Annual Value		1,28,250
Less: Deductions under section 24		
Standard Deduction (30% of Net Annual Value)	38,475	
Interest on borrowed capital proportionate to let-out portion ($₹24,000 \times 50/100$)	12,000	50,475
Income from Let-out Portion		77,775

5. *Computation of Gross Annual Value for let-out Portion of Mumbai Property*

	₹
Step One – Calculation of Notional Rent	
Municipal Value (Not available) or Fair Rental Value (Not available), whichever is higher = Not applicable	1,32,000
Or	
Standard Rent ($₹11,000 \times 12$) = ₹1,32,000.	
Since, the standard rent is given for each floor, the proportionate notional rent is the same as notional rent	
Step Two – Calculation of Rent Recovered	
Actual Rent per annum ($₹10,000 \times 12$)	₹1,20,000
Less: Unrealised Rent	Nil
Step Three – Calculation of Gross Annual Value	
Higher of steps 1 and 2	₹1,32,000
Less: Vacancy period rent	–

Illustration 23**Problem on computing income from property outside India, deciding on self-occupied and deemed to be let out properties and Arrears of Rent u/s 25A**

Mrs. Rohni Ravi, a citizen of USA, is a resident and ordinarily resident in India during the financial year 2017-18. She owns a house property at Los Angeles, USA, which is used as her residence. The annual value of the house is \$ 20,000. The value of one USD (\$) may be taken as ₹60.

She took ownership and possession of a flat in Chennai on 01-07-2017, which is used for self-occupation, while she is in India. The flat was used by her for 7 months only during the year ended 31-03-2018. Whilst the municipal valuation is ₹32,000 per month, the fair rent is ₹4,20,000 per annum. She paid the following to Corporation of Chennai:

10.50 • Income Tax - I

Property Tax ₹16,200

Sewerage Tax ₹1,800

She had taken a loan from Standard Chartered Bank for purchasing this flat. Interest on loan was as under:

Period prior to 01-04-2017 ₹49,200

01-04-2017 to 30-06-2017 ₹50,800

01-07-2017 to 31-03-2018 ₹1,31,300

She had a house property in Bangalore, which was sold in March 2017. In respect of this house, she received arrears of rent of ₹60,000 in March, 2018. This amount has not been charged to tax earlier.

Compute the income chargeable from house property of Mrs. Rohini Ravi for the assessment year 2018-19, exercising the most beneficial option available.

Solution:

The assessee has two properties – one in Los Angeles, USA and the other in Chennai, India. Both the properties are self-occupied. However, according to Income Tax Provisions, only one of them must be assessed as ‘Self-occupied Property’ and the other property must be assessed as ‘Deemed to be Let out Property’.

Since, the assessee has not given her option, the following options are available:

Option 1: To assess USA Property as Self-occupied property and Indian Property as ‘Deemed to be Let out’.

Option 2: To assess Indian Property as Self-occupied property and USA Property as ‘Deemed to be Let out’.

The taxable income from house properties, under both options, have been summarised in the following table:

Particulars	Option 1 (USA Property is Self-occupied Property) ₹	Option 2 (Indian Property is Self-occupied Property) ₹
Income from Property in USA (See Working Note below)	Nil	8,40,000
Income from Property in India (See Working Note below)	16,060	(-) 1,91,840
	16,060	6,48,160
Add Arrears of Rent under section 25A		
Arrears of rent received ₹60,000		
Less: Standard Deduction u/s 24(a) (₹60,000 × 30/100)	₹18,000	42,000
	58,060	6,90,160

Since the taxable income is lower under Option 1, it is advisable to assess the property in USA as 'self-occupied property' and the property in India as 'Deemed to be let-out property'.

Working Notes:

	Property in USA ₹	Property in India ₹
When the property is assessed as self-occupied property		
Annual Value	Nil	Nil
Less: Deduction under section 24(b)		
There is no loan details provided for property in USA.		
For property in Chennai , the interest as per format is–		
Previous year interest (₹ 50,800 + ₹ 1,31,300 = ₹ 1,82,000) plus Pre-completion period interest ($1/5 \times ₹ 49,200 = ₹ 9840$) = ₹ 1,91,840		
Or		
Maximum Limit = ₹ 2,00,000		
Whichever is lower.	Nil	1,91,840
	Nil	(–) 1,91,840
When the property is assessed as deemed to be let out property		
Gross Annual Value (See Note below)	12,00,000	3,15,000
Less: Municipal Taxes paid by the <i>assessee</i> during <i>previous year</i>	Nil	18,000
Net Annual Value	12,00,000	2,97,000
Less: Deductions under section 24		
(c) Standard Deduction (30% of Net Annual Value)	(–) 3,60,000	(–) 89,100
(d) Interest on borrowed capital	Nil	(–) 1,91,840
	8,40,000	16,060

Note:

For property in USA, the value has been given as 20,000\$ per annum. So, at the rate of ₹ 60 per \$, the annual value is $(20,000 \times ₹ 60) = ₹ 12,00,000$.

For property in India, the gross annual value is calculated as follows:

The assessee becomes owner of the property during previous year on 1st July 2017. She is owner only for 9 months during previous year. Hence, the Gross Annual Value (which is notional rent itself, in case of deemed to be let-out property) is calculated only for 9 months:

Municipal Value (₹ 32,000 \times 9 = ₹ 2,88,000) or Fair Rental Value (₹ 4,20,000 \times 9/12 = ₹ 3,15,000), whichever is higher = ₹ 3,15,000.

Or

Standard Rent (not applicable)

Whichever is less.

Since, Standard Rent is not applicable, the notional rent is ₹3,15,000. Hence, Gross Annual Value for the property in India, if it is assessed as deemed to be let out property, is **₹3,15,000**.

ADDITIONAL PROBLEMS UNDER THE HEAD INCOME FROM HOUSE PROPERTY

Illustration 24 Problem on Calculation of Gross Annual Value

Calculate the Gross Annual Value for Assessment Year 2018-19 in the following cases:

Particulars	HP 1	HP 2
Municipal Value	61,000	61,000
Fair Rental Value	72,000	72,000
Standard Rent	60,000	60,000
Monthly Rent – From 1-4-2017 to 30-6-2017	5,000	2,000
From 1-10-2017 to 31-3-2018	9,000	2,500
Vacancy Period	1 st July 2017 to 30 th September 2017	

Solution:

Calculation of Gross Annual Value

Particulars	HP 1	HP 2
Municipal Value	61,000	61,000
Fair Rental Value	72,000	72,000
Higher of the above	72,000	72,000
Standard Rent	60,000	60,000
Lower of the above = Notional Rent/Reasonable Expected Rent	60,000	60,000
Actual Rent/Rent Recovered	96,000	28,500
Higher of the above	96,000	60,000
Less: Vacancy Period Rent	27,000	7,500
Gross Annual Value	69,000	52,500

Working Notes:

Calculation of Actual Rent

$$\text{HP 1} = \{(5,000 \times 3) + (9,000 \times 9)\} = 96,000$$

$$\text{HP 2} = \{(2,000 \times 3) + (2,500 \times 9)\} = 28,500$$

Vacancy Period Rent (It is assumed that the higher rent is the rent of vacancy period)

$$\text{HP 1} = 9,000 \times 3 = 27,000$$

$$\text{HP 2} = 2,500 \times 3 = 7,500$$

Illustration 25 Problem on Computation of Income from Let out Property

Municipal Value ₹1,20,000; Fair Rental Value ₹1,30,000; Standard Rent ₹1,10,000; Annual Rent ₹1,26,000; Unrealised Rent ₹10,500; Municipal Taxes paid by the landlord during the year ₹17,000; Vacancy Period 1 month. Compute income from house property for Assessment Year 2018-19.

(Bangalore University, B.Com., November 2014)

Solution:

In this problem, unrealized rent & vacancy period is given. Hence, first we have to calculate actual rent recovered as under:

$$\begin{aligned}
 &= \text{Annual Rental Value} - \text{Unrealized rent} \\
 &= 1,26,000 - 10,500 \\
 &= 1,15,500.
 \end{aligned}$$

Calculation of Gross Annual Value

Particulars	₹
Municipal Value	1,20,000
Fair Rental Value	1,30,000
Higher of the above	1,30,000
Standard Rent	1,10,000
Lower of the above = Notional Rent/Reasonable Expected Rent	1,10,000
Actual Rent/Rent Recovered	1,15,500
Higher of the above	1,15,500
Less: Vacancy Period Rent ($\text{₹}1,26,000 \times 1/12$)	10,500
Gross Annual Value	1,05,000

Computation of Income from Let-out House Property

Particulars	₹	₹
Gross Annual Value		1,05,000
Less: Municipal Taxes paid by the Landlord		17,000
Net Annual Value		88,000
Less: Deductions u/s 24		
Standard deduction – 30% of Annual Value	26,400	
Interest on borrowed capital		
For Current Previous Year	–	
For Pre-Construction Period	–	26,400
Income from house property		61,600

Illustration 26 Problem on Computation of Income from Self-occupied and Deemed to be Let-out Properties

Mr. A has occupied 2 houses for his residential purposes particulars of which are as under:

Particulars	HP 1	HP 2
Municipal Value	30,000	90,000
Fair Rental Value	28,000	95,000
Standard Rent	20,000	80,000
Municipal Taxes paid	3,000	9,000
Interest on borrowed capital	900	1,500
Repairs	—	5,000

Determine Mr. A's Income from House Property for Assessment Year 2018-19.

Solution:

In this problem, it is given that Mr. A has occupied 2 houses for his residential purpose. An assessee can claim only one house property of his choice as self-occupied for residence (SOPR) and the other house shall be treated as “Deemed to be let out property” (DLOP). Since, the choice of the assessee is not mentioned in the problem, the property with higher rental value is *assumed* as the choice of the assessee and the other house is treated as “Deemed to be let out property”. The Gross Annual Value of “Deemed to be let out property” shall be arrived at as follows:

Calculation of Gross Annual Value

Particulars	₹
Municipal Value	30,000
Fair Rental Value	28,000
Higher of the above	30,000
Standard Rent	20,000
Lower of the above = Gross Annual Value	20,000

Computation of income from house property

Particulars	DLOP	SOPR
Gross Annual Value	20,000	—
Less: Municipal Taxes paid by the Landlord	3,000	—
Net Annual Value	17,000	Nil
Less: Deductions u/s 24		
(a) Standard deduction – 30% of Annual Value	5,100	—
(b) Interest on borrowed capital		
For Current Previous Year	900	1,500
For Pre-Construction Period	—	—
Income from house property	11,000	(1,500)

Total Income from house property = 11,000 – 1,500 = 9,500

Notes:

1. In the absence of specific information, the interest on loan is considered as interest for current previous year.
2. Since repairs are not allowed as deduction, it is ignored.

Illustration 27 Problem on calculation of Interest deductible u/s 24(b)

Mr. S borrowed a sum of ₹ 16,86,000 on 1-8-2014 for the construction of a house for self-occupied residence. The rate of interest is 9.6% p.a. The construction of the house was completed on 7th August, 2016. During the Previous Year 2017-18 the outstanding loan amount was ₹ 16,20,000. Find out the amount of interest that can be claimed as deduction u/s 24(b) for Assessment Year 2018-19.

Solution:

For calculation of interest for pre-construction period, first of all pre construction period shall be calculated. Since the loan amount is not yet fully repaid, the pre-construction period will be Date of Borrowing to 31st March, immediately preceding the Date of Construction i.e., 1/8/2014 to 31/3/2016 = 20 months.

(a) Interest for Current Previous Year = $16,20,000 \times 9.6\% = 1,55,520$

(b) Interest for Pre-Construction Period = $16,86,000 \times 9.6\% \times 20/12 \times 1/5 = 53,952$

Amount of interest that can be claimed as deduction u/s 24(b)

- The house property is meant for self-residence.
- The date of borrowing of loan is after 1/4/1999.
- Construction is completed **within 5 years from the end of the Financial Year** in which the loan was borrowed.
- Total interest on borrowed capital is ₹ 2,09,472 (i.e., 1,55,520 + 53,952).
- Therefore, the amount of interest that can be claimed is actual interest or maximum limit of ₹ 2,00,000 whichever is lower.
- Hence, the deduction that can be claimed u/s 24(b) is **₹ 2,00,000** being lower of the two.

Illustration 28 Problem on calculation of Interest deductible u/s 24(b)

Mr. T borrowed a sum of ₹ 12,86,000 on 1-8-2011 for the construction of a house for self-occupied residence purpose. The rate of interest is 9.6% p.a. The construction of the house was completed on 10th February, 2015. During Previous Year 2017-18 the outstanding loan amount was ₹ 11,60,000. Find out the amount of interest that can be claimed as deduction u/s 24(b) for Assessment Year 2018-19.

Solution

For calculation of interest for pre-construction period, first of all pre-construction period shall be calculated. Since the loan amount is not yet fully repaid, the pre-construction period will be

Date of Borrowing to 31st March, immediately preceding the Date of Construction i.e., 1/8/2011 to 31/3/2014 = 32 months.

(a) Interest for Current Previous Year = $11,60,000 \times 9.6\% = 1,11,360$

(b) Interest for Pre-Construction Period = $12,86,000 \times 9.6\% \times 32/12 \times 1/5 = 65,843$

Amount of interest that can be claimed as deduction u/s 24(b)

- The house property is meant for self-residence.
- The date of borrowing of loan is after 1/4/1999.
- Construction is completed **within 5 years from the end of the Financial Year** in which the loan was borrowed.
- Total interest on borrowed capital is ₹1,77,203 (i.e., 1,11,360 + 65,843).
- Therefore, the amount of interest that can be claimed is actual interest or maximum limit of ₹2,00,000 whichever is lower.
- Hence, the deduction that can be claimed u/s 24(b) is **₹1,77,203** being lower of the two.

Illustration 29 Problem on calculation of Interest deductible u/s 24(b)

Mr. U borrowed a sum of ₹8,46,000 on 1-10-2012 for the construction of a house for self-occupied residence. The rate of interest is 9.6% p.a. The construction of the house was completed on 31st March, 2016. During Previous Year 2017-18 the outstanding loan amount was ₹6,20,000. Find out the amount of interest that can be claimed as deduction u/s 24(b) for Assessment Year 2018-19.

Solution:

For calculation of interest for pre-construction period, first of all pre construction period shall be calculated. Since the loan amount is not yet fully repaid, the pre-construction period will be Date of Borrowing to 31st March, immediately preceding the Date of Completion i.e., 1/10/2012 to 31/3/2016 = 30 months.

(a) Interest for Current Previous Year = $6,20,000 \times 9.6\% = 59,520$

(b) Interest for Pre-Construction Period = $8,46,000 \times 9.6\% \times 30/12 \times 1/5 = 40,608$

Amount of interest that can be claimed as deduction u/s 24(b)

- The house property is meant for self residence.
- The date of borrowing of loan is after 1/4/1999.
- Construction is completed **within 5 years from the end of the Financial Year** in which the loan was borrowed.
- Total interest on borrowed capital is ₹1,00,128 (i.e., 59,520 + 40,608).
- Therefore, the amount of interest that can be claimed is actual interest or maximum limit of ₹2,00,000 whichever is lower.
- Hence, the deduction that can be claimed u/s 24(b) is **₹1,00,608** being lower of the two.

Illustration 30 Problem on Computation of Income from Let out Property

Mr. V borrowed a sum of ₹13,64,000 on 1-12-2012 for the construction of a house. The rate of interest is 9.6% p.a. The construction of the house was completed on 1st April, 2016 and let out since then on a monthly rent of ₹12,000. An amount of ₹46,000 was repaid towards the housing loan on 31-03-2017. Municipal tax paid is ₹14,000. Find out the income from house property for Assessment Year 2018-19.

Solution:**Computation of income from house property**

Particulars	₹	₹
Gross Annual Value (12,000 × 12)		1,44,000
Less: Municipal Taxes paid by the Landlord		14,000
Net Annual Value		1,30,000
Less: Deductions u/s 24		
(a) Standard deduction – 30% of Annual Value	39,000	
(b) Interest on borrowed capital (see note 1)		
For Current Previous Year	1,26,528	
For Pre-Construction Period	87,296	2,52,824
Income from house property (Loss)		(1,22,824)

Notes:

1. Since the house is let out, the entire interest on borrowed capital is allowable as deduction u/s 24(b).
2. For calculation of interest for pre-construction period, first of all pre-construction period shall be calculated. Since the loan amount is not yet fully repaid, the pre-construction period will be Date of Borrowing to 31st March, immediately preceding the Date of Completion i.e., 1/12/2012 to 31/3/2016 = 40 months.
 - (a) Interest for Current Previous Year = $(13,64,000 - 46,000) \times 9.6\% = 1,26,528$
 - (b) Interest for Pre-Construction Period = $13,64,000 \times 9.6\% \times 40/12 \times 1/5 = 87,296$

Illustration 31 Problem on Computation of Income from Let out Property

Mr. W borrowed a sum of ₹13,86,000 on 1-12-2012 for the construction of a house. The rate of interest is 9.6% p.a. The construction of the house was completed on 31st July, 2016 and was let out since then on a monthly rent of ₹15,000.

An amount of ₹68,000 was repaid towards the housing loan on 31-03-2017. Municipal tax due but not paid is ₹12,000. Find out the income from house property for Assessment Year 2018-19.

Solution:**Computation of Income from House Property**

Particulars	₹	₹
Gross Annual Value (15,000 × 8)		1,20,000
Less: Municipal Taxes paid by the Landlord (see note 1)		—
Net Annual Value		1,20,000
Less: Deductions u/s 24		
(c) Standard deduction – 30% of Annual Value	36,000	
(d) Interest on borrowed capital (see note 2)		
For Current Previous Year	1,26,528	
For Pre-Construction Period	88,704	2,51,232
Income from house property (Loss)		(1,31,232)

Notes:

1. Municipal tax actually paid is deductible. If it is due but not paid it is not deductible.
2. Since the house is let out, the entire interest on borrowed capital is allowable as deduction u/s 24(b).
3. For calculation of interest for pre-construction period, first of all pre-construction period shall be calculated. Since the loan amount is not yet fully repaid, the pre-construction period will be Date of Borrowing to 31st March, immediately preceding the Date of Completion i.e., 1/12/2012 to 31/3/2016 = 40 months.
 - (a) Interest for Current Previous Year = $(13,86,000 - 68,000) \times 9.6\% = 1,26,528$
 - (b) Interest for Pre-Construction Period = $13,86,000 \times 9.6\% \times 40/12 \times 1/5 = 88,704$

Illustration 32 Problem on Computation of Income from Let out Property

Mrs. X started construction of her house on 07-06-2014 and took housing loan of ₹6,00,000 at 9.6% per annum on 01-07-2016. The construction of the house was completed on 22-06-2017 and was let out from 01-07-2017 on a monthly rent of ₹7,500. An amount of ₹68,000 was repaid towards the housing loan on 31-03-2018. Municipal tax paid ₹9,000. Find out the income from house property for Assessment Year 2018-19.

Solution:**Computation of Income from House Property**

Particulars	₹	₹
Gross Annual Value (7,500 × 9)		67,500
Less: Municipal Taxes paid by the Landlord		9,000

Particulars	₹	₹
Net Annual Value		58,500
Less: Deductions u/s 24		
(a) Standard deduction – 30% of Annual Value	17,550	
(b) Interest on borrowed capital (see note 2)		
For Current Previous Year	51,072	
For Pre-Construction Period	8,640	77,262
Income from house property (Loss)		(18,762)

Notes:

1. Since the house is let out, the entire interest on borrowed capital is allowable as deduction u/s 24(b).
2. For calculation of interest for pre-construction period, first of all pre-construction period shall be calculated. Since the loan amount is not yet fully repaid, the pre-construction period will be Date of Borrowing to 31st March, immediately preceding the Date of Completion i.e., 1/07/2016 to 31/3/2017 = 9 months.
 - (a) Interest for Current Previous Year = $(6,00,000 - 68,000) \times 9.6\% = 51,072$
 - (b) Interest for Pre-Construction Period = $6,00,000 \times 9.6\% \times 9/12 \times 1/5 = 8,640$

Illustration 33 **Problem on Computation of Income from Self-occupied and Deemed to be Let Out Properties**

Mr. B has occupied 3 houses for his residential purposes particulars of which are as under:

Particulars	HP 1	HP 2	HP 3
Municipal Value	10,000	30,000	30,000
Fair Rental Value	18,000	18,000	35,000
Standard Rent	15,000	20,000	NA
Municipal Taxes paid	1,200	2,400	3,600
Fire Insurance premium paid	1,200	900	500
Repairs	1,800	Nil	Nil
Ground Rent paid	500	700	Nil

Mr. B borrowed ₹ 30,000 at 12% p.a. on 1-06-2013 for the construction of HP 3 whose construction was completed on 10-05-2017. The entire loan amount was repaid on 31-01-2017. Determine Mr. B's Income from House Property for Assessment Year 2018-19.

Solution:

In this problem, it is given that Mr. B has occupied 3 houses for his residential purpose. An assessee can claim only one house property of his choice as self-occupied for residence (SOPR) and the other houses shall be treated as “Deemed to be let out property” (DLOP). Since, the choice of the

assessee is not mentioned in the problem, the property with higher rental value will be considered as the choice of the assessee and the other house shall be treated as “Deemed to be let out property”. The third house property is considered as Self occupied for residence and the Gross Annual Value of the other two “Deemed to be let out properties” shall be arrived at as follows:

Calculation of Gross Annual Value

Particulars	HP 1	HP 2
Municipal Value	10,000	30,000
Fair Rental Value	18,000	18,000
Higher of the above	18,000	30,000
Standard Rent	15,000	20,000
Lower of the above = Gross Annual Value	15,000	20,000

Computation of Income from House Property

	HP 1 DLOP	HP 2 DLOP	HP 3 SOPR
Gross Annual Value	15,000	20,000	–
Less: Municipal Taxes paid by the Landlord	1,200	2,400	–
Net Annual Value	13,800	17,600	Nil
Less: Deductions u/s 24			
(a) Standard deduction – 30% of Annual Value	4,140	5,280	–
(b) Interest on borrowed capital			
For Current Previous Year	–	–	–
For Pre-Construction Period	–	–	2,640
Income from house property	9,660	12,320	(2,640)

Total Income from house property = 9,660 + 12,320 – 2,640 = 19,340.

Notes:

- For calculation of interest for pre-construction period, first of all pre-construction period shall be calculated. Since the loan amount is fully repaid, the pre-construction period will be Date of Borrowing to 31st March, immediately preceding the Date of Completion i.e., 1/06/2013 to 31/3/2017 = 46 months OR Date of borrowing to Date of repayment of loan i.e., 1/06/2013 to 31/01/2017 = 44 months whichever is earlier. Therefore, pre-construction interest is to be calculated considering 44 months being earlier.
 - Interest for Current Previous Year = Nil as the entire amount is repaid before 1/4/2017.
 - Interest for Pre-Construction Period = $30,000 \times 12\% \times 44/12 \times 1/5 = 2,640$.
- Fire Insurance premium paid, Repairs & Ground Rent paid are not eligible for deduction u/s 24. Hence, they are ignored.

Illustration 34 Problem on Computation of Income from Let-out and Self-occupied Properties

Mr. C is the owner of 3 houses one each at Mysore, Davanagere and Bijapur. Mysore house is occupied by him for his residential purpose. Davanagere house is let out to a lawyer for residential purpose and Bijapur house is let out to a businessman for use as godown. Following particulars are available with respect to these properties:

Particulars	Mysore	Davanagere	Bijapur
Municipal Value	2,36,000	1,42,000	1,60,000
Fair Rental Value	2,38,000	1,40,000	1,64,000
Annual Rent receivable	–	1,50,000	1,60,000
Standard Rent	–	1,41,000	1,62,000
Municipal Taxes paid	3,600	14,200	16,000
Interest on borrowed capital	1,18,000	40,000	1,00,000
Vacancy period	–	1 month	–

Determine Mr. C's Income from House Property for Assessment Year 2018-19.

Solution:**Calculation of Gross Annual Value**

Particulars	Davanagere	Bijapur
Municipal Value	1,42,000	1,60,000
Fair Rental Value	1,40,000	1,64,000
Higher of the above	1,42,000	1,64,000
Standard Rent	1,41,000	1,62,000
Lower of the above = Notional Rent/Reasonable Expected Rent	1,41,000	1,62,000
Actual Rent/Rent Recovered	1,50,000	1,60,000
Higher of the above	1,50,000	1,62,000
Less: Vacancy Period Rent	12,500	–
Higher of the above = Gross Annual Value	1,37,500	1,62,000

Computation of Income from House Property

Particulars	Mysore	Davanagere	Bijapur
Gross Annual Value	–	1,37,500	1,62,000
Less: Municipal Taxes paid by the Landlord	–	14,200	16,000

Net Annual Value	Nil	1,23,300	1,46,000
Less: Deductions u/s 24			
Standard deduction – 30% of Annual Value	–	36,990	43,800
Interest on borrowed capital	1,18,000	40,000	1,00,000
Income (Loss) from house property	(1,18,000)	46,310	2,200

Total Income (Loss) from house property = 46,310 + 2,200 – 1,18,000 = (69,490).

Illustration 35 Problem on Computation of Income from Let-out, Self-occupied and Deemed to be Let Out Properties

Mr. F owns 4 houses. House property 1 is let out for business purpose, house property 2 is occupied for own business and house properties 3 and 4 are occupied for own residence. Following particulars are available with respect to these properties.

Particulars	HP 1	HP 2	HP 3	HP 4
Municipal Value	1,30,000	15,000	1,68,000	1,95,000
Fair Rental Value	1,39,000	28,000	1,77,000	1,95,000
Standard Rent	1,36,200	22,000	1,75,000	1,90,000
Annual Rent	1,42,800	–	–	–
Unrealised Rent	13,500	–	–	–
MT paid by Mr. F	–	2,500	17,000	19,000
MT paid by Tenant	13,000	–	–	–
Date of completion of construction	31-5-15	31-05-15	31-03-15	31-03-14

House Property 1 remained vacant for 2 months from March 16, 2018. Mr. F borrowed ₹3,00,000; ₹4,00,000 and ₹6,50,000 respectively for the construction of HP 1, HP 3 and HP 4. (Date of borrowing: HP 1 June 1, 2013; HP 3 August 1, 2014; HP 4 October 1, 2014. Date of repayment of all loans together with interest 31-12-2017. Rate of interest on all loans 15% p.a. Determine Mr. F's Income from House Property for Assessment Year 2018-19.

Solution:

1. House property used for own business is not assessed under the head income from house property. Hence, house property 2 shall be ignored.
2. Of the two house properties occupied for self-residence, one house property shall be treated as “deemed to be let out”. House property no. 3 should be treated as “deemed to be let out” since it has lower rental value compared to the house property no. 4
3. The Gross Annual Value of house properties no. 1 and 3 is arrived at as follows:

Calculation of Gross Annual Value

Particulars	HP 1 (LOP)	HP 3 (DLOP)
Municipal Value	1,30,000	1,68,000
Fair Rental Value	1,39,000	177,000
Higher of the above	1,39,000	1,77,000
Standard Rent	1,36,200	1,75,000
Lower of the above = Notional Rent/Reasonable Expected Rent	1,36,200	1,75,000
Actual Rent/Rent Recovered	1,42,800	–
Higher of the above	1,42,800	–
Less: Vacancy Period Rent	5,950	–
Gross Annual Value	1,36,850	1,75,000

Note:

Vacancy Period Rent

$$= \{1,42,800/12\} \times \frac{1}{2} \text{ } ^*$$

$$= ₹ 5,950$$

* Vacancy period is only for ½ month as the house property is vacant from 16th March to 31st March, 2018 during the current Previous Year 2017-18.

Computation of income from house property

Particulars	HP 1 (LOP)	HP 3 (DLOP)	HP 4 (SOPR)
Gross Annual Value	1,36,850	1,75,000	–
Less: Municipal Taxes paid by the Landlord	–	17,000	–
Net Annual Value	1,36,850	1,58,000	Nil
Less: Deductions u/s 24			
(a) Standard deduction – 30% of Annual Value	41,055	47,400	–
(b) Interest on borrowed capital			
For Current Previous Year	33,750	45,000	73,125
For Pre-Construction Period	25,500	8,000	–
Income (Loss) from house property	36,545	57,600	(73,125)

$$\text{Total Income (Loss) from house property} = 36,545 + 57,600 - 73,125 = 21,020.$$

Note on interest on borrowed capital:**HP 1**

Pre-construction period = Date of Borrowing to 31st March, immediately preceding the Date of Completion i.e., 1/06/2013 to 31/3/2016 = 34 months OR Date of borrowing to Date of repayment

of loan i.e., 1/06/2013 to 31/12/2017 = 55 months whichever is earlier. Therefore, pre-construction interest is to be calculated considering 34 months being earlier.

Interest for Current Previous Year = $3,00,000 \times 15\% \times 9/12 = 33,750$

Interest for Pre-Construction Period = $3,00,000 \times 15\% \times 34/12 \times 1/5 = 25,500$.

HP 3

Pre-construction period = Date of Borrowing to 31st March, immediately preceding the Date of Completion i.e., 1/8/2014 to 31/3/2015 = 8 months OR Date of borrowing to Date of repayment of loan i.e., 1/8/2014 to 31/12/2017 = 41 months whichever is earlier. Therefore, pre-construction interest is to be calculated considering 8 months being earlier.

Interest for Current Previous Year = $4,00,000 \times 15\% \times 9/12 = 45,000$

Interest for Pre-Construction Period = $4,00,000 \times 15\% \times 8/12 \times 1/5 = 8,000$.

HP 4

Pre-construction period = Date of Borrowing to 31st March, immediately preceding the Date of Completion i.e., 1/10/2014 to 31/3/2014 = Zero months (since the 31st March, immediately preceding the date of completion is earlier to the date of borrowing) OR Date of borrowing to Date of repayment of loan i.e., 1/10/2014 to 31/12/2017 = 39 months whichever is earlier. Therefore, pre-construction interest is to be calculated considering Zero months being earlier.

Interest for Current Previous Year = $6,50,000 \times 15\% \times 9/12 = 73,125$

Interest for Pre-Construction Period = $6,50,000 \times 15\% \times 0/12 \times 1/5 = \text{Zero}$.

Illustration 36 Problem on Computation of Income from Let-out and Self-occupied Properties

Mr. Raphael constructed a shopping complex. He had taken a loan of ₹25 Lakhs for construction of the said property on 01-08-2015 from SBI @ 10% for 5 years. The construction was completed on 30-06-2016. Rental income from shopping complex ₹30,000 per month – let out for the whole year. Municipal Taxes paid for shopping complex ₹8,000.

Arrears of rent received from shopping complex ₹1,20,000.

Interest paid on loan taken from SBI for purchase of house for use as own residence for the period 2017-18, ₹3 Lakhs.

You are required to compute Income from House Property of Mr. Raphael for Assessment Year 2018-2019 as per Income Tax Act, 1961.

Solution:

Computation of Income from House Property

	₹	₹
Income from Letting Out Shopping Complex (See Working Note below)		47,067
Income from Self-occupied Property (See Working Note below)		(2,00,000)
Income from House Property		(1,52,933)

Let-out Property		
Gross Annual Value (In the absence of other information, rent charged itself is taken as Gross Annual Value – ₹30,000 × 12)		3,60,000
Less: Municipal Taxes <i>paid</i> by the <i>assessee</i> during the <i>previous year</i> .		8,000
Net Annual Value		3,52,000
Less: Deductions under section 24		
(a) Standard Deduction (30% of Net Annual Value)	1,05,600	
(b) Interest on borrowed capital (See Working Note below)	2,83,333	3,88,933
		(36,933)
Add: Arrears of Rent under section 25B		
Arrears of Rent Received	1,20,000	
Less: Standard Deduction @ 30%	36,000	84,000
		47,067
Self-Occupied Property		
Gross Annual Value		Nil
Less: Deduction under section 24(b)		
Interest for relevant previous year (2017-18)	3,00,000	
Or		
Maximum Limit	2,00,000	
Whichever is less		2,00,000
		(2,00,000)

Notes:**Interest on Borrowed Capital:**

	₹
Previous Year Interest (See Point (i) below)	2,50,000
Add: One-fifth of 'Pre-completion period interest' (See Points (ii) and (iii) below) (₹1,66,667 × 1/5)	33,333
Interest deductible under section 24(b)	2,83,333

Explanation:

- (i) The relevant previous year is 2017-18. Out of loan amount of ₹25,00,000 borrowed no repayment is made before 1st April 2017. (Based on the statement in the problem, it can be assumed that entire loan will be repaid after 5 years).

So, the loan amount outstanding during previous year 2017-18 is ₹25,00,000.

Accordingly, the interest for previous year 2017-18 is:

$$(\text{₹}25,00,000 \times 10/100) = \text{₹}2,50,000.$$

- (ii) The loan was borrowed on 1st August 2015, the construction of the property was completed on 30th June, 2016.

The starting date of pre-completion period is 1st August 2015.

The ending date of pre-completion period is **earlier** of 31st March preceding the date of completion of construction (i.e., 31st March 2016) or date on which loan has been completely repaid (No repayment till date). The earlier of the two is 31st March 2016.

So, the 'pre-completion period' is 1st August 2015 to 31st March 2016 (8 months).

During the above period of 8 months, no repayments have been made.

So, the loan amount outstanding during 'pre-completion period' is:

Accordingly, 'pre-completion period interest' is:

$$(\text{₹}25,00,000 \times 10/100 \times 8/12) = \text{₹}1,66,667$$

- (iii) The construction being completed during previous year 2016-17, the deduction for 'pre-completion period interest' is available for previous years 2016-17, 2017-18, 2018-19, 2019-20 and 2020-21. Since, the relevant previous year of the assessee (2017-18) is one among the above five years, deduction for pre-construction period must be considered.

SUMMARY

- An income is chargeable under the head "Income from House Property" when the income is from a property which can be considered under the head "House Property".
- A property can be considered under the head "Income from House Property" when it fulfills 3 conditions viz., (a) the property consists of buildings and land appurtenant thereto, (b) it is owned by the assessee, and (c) it is not used by the assessee for his own business or profession.
- Computing taxable income from house property depends upon the usage of property. Based on usage, properties are classified into broadly four types viz., Let-out Property, Self-occupied property (for residence), Deemed to be let out property, and partly-let-out & partly-self-occupied property.
- In case of Let-out Property, the taxable income can be arrived at by providing deductions u/s 24 from 'Net Annual Value'.
- 'Net Annual Value' = Gross Annual Value **minus** Municipal Taxes paid by assessee during previous year.
- In case of Let-out property, 'Gross Annual Value' is considered as **higher** of 'Notional Rent' and 'Rent received', **minus** Vacancy Period Rent.
- 'Notional Rent' is higher of Municipal Value and Fair Rental Value, restricted to Standard Rent.
- 'Rent Received' = Actual Rent per annum **minus** Unrealised Rent.
- There are two deductions u/s 24 – (a) Standard Deduction and (b) Interest on Borrowed Capital.

- Standard Deduction u/s 24(a) is 30% of 'Net Annual Value'. It is deductible towards expenses incurred by the owner on the property. It must be deducted to the said extent, irrespective of the actual expenditure incurred on the property.
- Interest on borrowed capital u/s 24(b) is deductible only when the loan is borrowed for purchase, construction, repair, renewal, etc., of the property.
- Under section 24(b), the amount of interest deductible = Previous Year Interest + $\frac{1}{5}$ th of Pre-completion period interest.
- After providing deductions u/s 24 from 'Net Annual Value', any positive balance represents 'Income from House Property' and any negative balance represents 'Loss from House Property'.
- In case of 'Self-occupied Property', the taxable income is calculated by providing Deduction u/s 24(b) from 'Annual Value'.
- For a Self-occupied Property, the 'Annual Value' is **Nil**.
- The amount of deduction u/s 24(b) for a 'Self-occupied property' is restricted. The maximum deduction that can be claimed is ₹2,00,000 (on fulfillment of 3 conditions) or ₹30,000 (on non-fulfillment of any or all of the 3 conditions).
- When an assessee who owns more than one house property, occupies more than one property for self-occupation – only one must be assessed as 'Self-occupied Property' and the remaining self-occupied properties must be assessed as 'Deemed to be Let-out Property'.
- The format and provisions for 'Deemed to be Let out Property' is same as in the case of Let out Property. The only difference is in Computation of Gross Annual Value. For a deemed to be let-out property, Notional Rent itself will be considered as Gross Annual Value.
- An assessee might use a portion of property for self-occupation and let-out the remaining portion. Alternatively, the assessee might let-out the property for a certain period during the previous year, and occupy for self for the remaining period. Such cases are called as "Partly-let-out and partly-self-occupied".
- Where a property is "portion let-out and portion self-occupied", for each portion taxable income must be calculated using the respective provisions (i.e., let out property provisions for let-out portion, and self-occupied property provisions for self-occupied portion), and consolidated.
- Where a property is "period let-out and period self-occupied", it must be assessed as a let-out property.
- Any unrealised rent recovered during previous year, or any arrears of rent received during previous year, must be taxable u/s 25A after providing for Standard Deduction u/s 24(a).
- When a property has more than one owner, the income from house property must be distributed among each owner in the proportion of their ownership.
- A property located in a foreign country and owned by the assessee, must be assessed on similar lines of property located in India.

THEORY QUESTIONS

Section A Type Questions

1. State the chargeability under the head 'Income from House Property'.
2. What is the meaning of the term 'land appurtenant thereto'?

3. What is the basis of charge under this head of income?
4. State the different types of house property, for the purpose of computing taxable income.
5. What is Gross Annual Value?
6. Define Annual Value (Bangalore University, B.Com., Nov/Dec 2014)
7. State the meaning of Annual Value (Bangalore University, B.Com., Nov/Dec 2015)
8. What is Standard Rent (Bangalore University, B.Com., Nov/Dec 2014) (Nov/Dec 2016)
9. What do you mean by pre-construction period? (Bangalore University, B.Com., Nov/Dec 2017)
10. How is notional or expected rent calculated?
11. What is unrealised rent? What are the conditions for deducting unrealised rent?
12. What is vacancy period rent?
13. What is standard rent?
14. List the conditions for deduction of municipal tax from 'gross annual value'.
15. List the deductions under section 24.
16. What is 'standard deduction'? For what purpose is the deduction given?
17. What is the format for calculating 'interest on borrowed capital'?
18. What is 'previous year interest'? On what basis, is it deductible?
19. What is pre-completion period interest? How is pre-completion period identified?
20. What is the maximum limit for deduction under section 24(b) in case of self-occupied properties?
21. What are 'deemed to be let out properties'?
22. What is co-ownership? What is the tax treatment for a property which is co-owned?
23. What is the treatment for recovery of unrealised rent pertaining to previous year 2000-01 or earlier years?
24. What is the treatment for recovery of unrealised rent pertaining to previous year 2001-02 or later years?
25. What is 'arrears of rent'? What is its tax treatment?
26. List the various cases of deemed ownership.
27. What is the tax provision when the ownership of a property is in dispute?
28. What is the tax treatment for property let out by the assessee to his employees?
29. What is the tax treatment for 'properties held as stock-in-trade' and 'income from providing paying guest accommodation'?

Section B Type Questions

1. Explain in detail the conditions for considering an income under the head 'income from house property'.
2. Explain in detail the provisions under section 24(b) – deduction for 'interest on borrowed capital'.
3. Explain the tax provisions for 'unrealised rent recovered' under section 25AA.
4. Explain in detail, the tax treatment for 'arrears of rent received' under section 25B.
5. Explain in detail the exceptions for the condition that 'assessee must be owner of the property'.

EXERCISES

1. Calculate Notional Rent in the following cases:

Particulars	HP 1	HP 2	HP 3	HP 4	HP 5
Municipal Value	40,000	40,000	40,000	40,000	40,000
Fair Rental Value	46,000	46,000	46,000	48,000	51,000
Standard Rent	NA	45,000	35,000	45,000	63,000

(Ans: ₹46,000, ₹45,000, ₹35,000, ₹45,000 and ₹51,000)

2. Calculate the Gross Annual Value in the following cases:

Particulars	HP 1	HP 2	HP 3	HP 4	HP 5	HP 6
Municipal Value	20,000	24,000	36,000	42,000	48,000	45,000
Fair Rental Value	24,000	24,000	40,000	42,000	50,000	50,000
Standard Rent	NA	24,000	50,000	30,000	NA	48,000
Annual Rent	18,000	36,000	48,000	36,000	54,000	42,000

(Ans: ₹24,000, ₹36,000, ₹48,000, ₹36,000, ₹54,000 and ₹48,000)

3. Calculate the Gross Annual Value in the following cases:

Particulars	HP 1	HP 2	HP 3	HP 4	HP 5
Municipal Value	60,000	60,000	60,000	1,12,000	1,12,000
Fair Rental Value	68,000	68,000	68,000	1,17,000	1,17,000
Standard Rent	62,000	62,000	70,000	1,15,000	1,15,000
Annual Rent	66,000	66,000	72,000	1,20,000	1,44,000
Unrealised Rent	2,000	6,000	5,000	50,000	12,000

(Ans: ₹64,000, ₹62,000, ₹68,000, ₹1,15,000 and ₹1,32,000)

4. Calculate the Gross Annual Value in the following cases:

Particulars	HP 1	HP 2	HP 3	HP 4	HP 5	HP 6	HP 7
Municipal Value	60,000	61,000	60,000	80,000	80,000	1,40,000	1,40,000
Fair Rental Value	65,000	66,000	64,500	78,000	78,000	1,50,000	1,50,000
Standard Rent	59,500	59,000	63,000	85,000	-----	1,20,000	1,20,000
Annual Rent	72,000	57,000	72,000	72,000	-----	96,000	1,44,000
Vacancy Period (months)	1	1 ½	5	3	-----	10	10

Note: HP 5 is self occupied for residence.

(Ans: ₹66,000, ₹51,875, ₹42,000, ₹67,000, ₹40,000 and ₹24,000)

5. Calculate the Gross Annual Value in the following cases:

Particulars	HP 1	HP 2	HP 3	HP 4	HP 5
Municipal Value	1,40,000	1,80,000	1,80,000	1,40,000	2,31,000
Fair Rental Value	1,45,000	1,85,000	1,85,000	1,45,000	2,62,000
Standard Rent	1,42,000	1,75,000	1,75,000	1,42,000	2,41,000
Annual Rent	1,68,000	1,68,000	1,68,000	1,68,000	2,52,000
Unrealised Rent	14,000	42,000	1,000	70,000	42,000
Vacancy Period (months)	$\frac{1}{2}$	1	1	3	5

(Ans: ₹1,47,000, ₹1,61,000, ₹1,61,000, ₹1,00,000 and ₹1,36,000)

6. Calculate Gross Annual Value from the following particulars:

- (a) Monthly Rent ₹8,500
- (b) Municipal Rent ₹65,000
- (c) Fair Rent ₹69,000
- (d) Standard Rent ₹55,000

The assessee could not realize rent for one month and the house also remained vacant for three months during the PY 2017-18.

(Nov/Dec 2014-BBM – Modified)

(Ans: ₹68,000)

7. From the following information compute Net Annual Value of House Property for the AY 2018-19:

- (a) Municipal Value ₹1,00,000
- (b) Fair Rental Value ₹1,80,000
- (c) Let out (per month) ₹16,000
- (d) Standard Rent ₹1,20,000
- (e) Unrealized rent for one month
- (f) Municipal tax paid by owner of house property ₹20,000
- (g) Municipal tax paid by tenant ₹10,000

(Bangalore University, B.Com., Nov/Dec 2016)

(Ans: ₹1,56,800)

8. Determine the Net Annual Value of the House Property for the AY 2018-19:

Municipal Value	₹1,50,000
Fair Rent	₹1,70,000
Standard Rent	₹1,30,000
Actual Rent per month	₹15,000
Unrealized Rent	₹18,000
House Vacancy Period	1 month
Municipal tax paid	₹15,000

(Bangalore University, B.Com., Nov/Dec 2017)

(Ans: 1,32,000)

9. Smt. Jaya is the owner of a house at Agra, particulars in respect of which for the year ended 31st March, 2018 are as below:

- (a) Actual rent received ₹1,00,000
- (b) Municipal valuation ₹80,000
- (c) Total Municipal Tax ₹25,000
- (d) Municipal Tax paid by Smt. Jaya ₹12,500
- (e) Municipal Tax paid by the tenant ₹12,500
- (f) Interest paid during PY on loan taken for renewing the house ₹40,000
- (g) Repair charges ₹3,00,000

Compute her income from house property for the AY 2018-19.

(Bangalore University, B.Com, Nov/Dec 2015 - Modified)

(Ans: ₹21,250)

10. Mr. Ravi (Resident) owns a building consisting of 3 houses. The particulars are as follows:

Particulars	House A ₹	House B ₹	House C ₹
Annual Fair Rent	40,000	35,000	50,000
Municipal Valuation	50,000	40,000	50,000
Standard Rent	45,000	42,000	55,000
Let out (per month)	3,000	2,000	—
Purpose of Use	LOP for Residence	LOP for Business	SOP for Residence
Repairs	2,000	1,000	—
Collection charges	3,000	1,000	—
Interest on loan	15,000	5,000	2,000

Municipal tax is 10% on Municipal Value. Municipal tax for House A was paid by tenant, for House B it was not paid till 31/3/2018 and for House C it was paid by the Owner. House A remained vacant for 4 months. Compute taxable income from house property for the AY 2018-19.

(Bangalore University, BBM, Nov/Dec 2014-Modified)

(Ans: House A – ₹8,100, House B – ₹23,000, House C – ₹2,000,
Total Income from House Property – ₹29,100)

11. Mr. Girish is the owner of following house property in Mysuru. Particulars in respect of which for the year ended 31/3/2018 are as follows:

Particulars	I House (LOP) ₹	II House (LOP) ₹	III House (Dwelling house) ₹
Annual rent for 12 months	24,000	18,000	Nil
Standard rent	18,000	12,000	Nil
Municipal value	16,000	14,000	35,600
Total municipal tax	1,600	1,400	3,560
Municipal tax paid by Girish	1,600	700	3,560

10.72 • Income Tax-I

Particulars	I House (LOP) ₹	II House (LOP) ₹	III House (Dwelling house) ₹
Municipal tax paid by tenant	Nil	700	Nil
Repairs	1,000	500	2,000
Vacancy period	2 months	Nil	Nil
Interest on loan for repairing house	800	600	2,000
Unrealized rent allowed in the AY 2015-16 recovered during the year.	4,000	Nil	Nil

Compute income from house property for the AY 2018-19.

(Bangalore University, B.Com, Nov/Dec 2015)

*(Ans: House I – ₹14,880, House II – ₹11,510, House III – ₹2,000,
Total Income from House Property – ₹24,390)*

12. Mr. Shankar is the owner of three house properties in Bengaluru and has let out all the houses throughout the year.

Particulars	House A ₹	House B ₹	House C ₹
Fair Rent	1,80,000	1,50,000	1,20,000
Municipal Valuation	1,50,000	2,00,000	1,00,000
Let out (per month)	20,000	15,000	25,000
Use by tenant	Residential	Office	Residential
Repair charges	10,000	–	40,000
Collection charges	20,000	5,000	–
Interest on loan			
For construction	1,00,000	–	–
For marriage of daughter	–	60,000	–
For repairs	–	–	10,000

Municipal tax is 10% of municipal valuation. Municipal tax of house A was paid by owner but municipal tax of house B was not paid upto 31st March 2018 and municipal tax of house C was paid by tenant. The house C remained vacant for 2 months during the PY. Compute income from house property for the AY 2018-19.

(Bangalore University, B.Com, Nov/Dec 2016)

*(Ans: House I – ₹57,500, House II – ₹1,40,000, House III – ₹1,65,000,
Total Income from House Property – ₹3,62,500)*

13. Mr. Suryakantha has three houses in Mandya and particulars of which are relating to the PY are as under:

Particulars	House I ₹	House II ₹	House III ₹
Use of house	Let out	Let out	Self occupied
Standard Rent	1,50,000	2,00,000	—
Municipal Value	1,00,000	3,00,000	3,00,000
Fair Rental Value	1,80,000	1,80,000	3,50,000
Actual rent per month	15,000	20,000	—
Municipal tax paid	10%	10%	10%
Repair charges	—	—	2,000

Suryakantha borrows ₹6,00,000 at 10% per annum from the bank for construction of house III (date of borrowing 1/6/2013 and date of repayment of entire amount of loan together with interest 30/9/2017). Construction of the house is completed in June 2016. Determine the taxable income from house property for the AY 2018-19.

(Bangalore University, B.Com, Nov/Dec 2016 - modified)

(Ans: House I – ₹1,19,000, House II – ₹1,47,000, House III – ₹64,000,
Total Income from House Property – ₹2,02,000)

14. Mr. Anand is owner of three houses in Bengaluru, the particulars of which are given below:

Particulars	House A ₹	House B ₹	House C ₹
Municipal Value	30,000	40,000	20,000
Fair Rent	36,000	30,000	24,000
Let out (per month)	4,000	3,000	5,000
Construction completed	1/4/2015	1/6/2015	31/3/2014
Repairs	—	5,000	4,000
Municipal tax paid by owner	3,000	—	—
Municipal tax paid by tenant	—	—	2,000
Municipal tax due	—	4,000	—
Vacancy period	—	—	2 Months

Anand took a loan of ₹3,00,000 at 8.5% per annum for construction of House B. Date of borrowing loan is 01/07/2012. Compute income from house property for the AY 2018-19.

(Bangalore University, B.Com, Nov/Dec 2017)

(Ans: House A – ₹31,500, House B – ₹11,525, House C – ₹35,000,
Total Income from House Property – ₹54,975)

15. Mr. Shankar owns three houses in KGF. From the following particulars compute his taxable income from house property for the AY 2018-19.

10.74 • Income Tax - I

Particulars	House I ₹	House II ₹	House III ₹
Municipal Value	60,000	90,000	65,000
Fair Rent	65,000	1,00,000	60,000
Rent received	—	88,000	—
Municipal tax paid at 10% of municipal value			
Repairs	1,000	8,000	6,000
Interest on loan take for house construction	—	10,000	8,000
How used	SOPR	LOP	SOPR

(Bangalore University, B.Com, Nov/Dec 2017)

*(Ans: House I – ₹41,300, House II – ₹53,700, House III – ₹8,000,
Total Income from House Property – ₹87,000)*

[Hint: It is advisable for Mr. Shankar to consider House I as Self-occupied Property for Assessment purposes]

Income Tax Authorities

CHAPTER OVERVIEW

- 11.1 Introduction
- 11.2 Central Board of Direct Taxes (CBDT)
- 11.3 Director General/Director
- 11.4 Commissioners of Income Tax
- 11.5 Commissioners (Appeals)
- 11.6 Joint Commissioners
- 11.7 Income Tax Officers
- 11.8 Inspectors of Income Tax

- • The Levy, Administration and Collection of
- Income Tax is carried out by various authorities
- constituted under the Income Tax Act. This
- chapter provides a brief outline of the various
- Income Tax Authorities and their powers.

INTRODUCTION

11.1

- The following authorities have been constituted
- under section 116 of the Income Tax Act, 1961
- to discharge the executive and administration

functions relating to income tax matters:

- A. The Central Board of Direct Taxes.
- B. Director-General of Income-tax or Chief Commissioners of Income-tax.
- C. Directors of Income-tax or Commissioners of Income-tax.
- D. Commissioners of Income-tax (Appeals).
- E. Additional Directors of Income-tax, Additional Commissioners of Income-tax, or Additional Commissioners of Income-tax (Appeals).
- F. Joint Directors of Income-tax or Joint Commissioner of Income-tax.
- G. Deputy Directors of Income-tax, Deputy Commissioners of Income-tax, or Deputy Commissioners of Income-tax (Appeals).
- H. Assistant Directors of Income-tax or Assistant Commissioners of Income-tax.
- I. Income-tax Officers.
- J. Tax Recovery Officers.
- K. Inspectors of Income-tax.

Note:

According to the respective definition under section 2:

- (a) 'Joint Commissioner' includes a Joint Commissioner of Income-tax or Additional Commissioner of Income-tax.
- (b) 'Joint Director' includes a Joint Director of Income-tax or Additional Director of Income-tax.
- (c) 'Assistant Commissioner' includes an Assistant Commissioner of Income-tax or Deputy Commissioner of Income-tax.
- (d) 'Assistant Director' includes an Assistant Director of Income-tax or Deputy Director of Income-tax.

CENTRAL BOARD OF DIRECT TAXES (CBDT)

11.2

The Central Board of Direct Taxes was constituted under the Central Boards of Revenue Act, 1963. The Act has assigned the following powers to the Board:

1. The CBDT may from time to time issue such orders, instructions and directions to other income-tax authorities as it may deem fit for the **proper administration** of the Act. Such authorities and other persons employed in the execution of the Act shall observe and follow such orders, instructions and directions of CBDT. However, the **CBDT is not empowered** to issue an order or direction or instruction for the following:
 - (a) so as to require any income-tax authority to make a particular assessment or dispose of a particular case in a particular manner,
 - (b) so as to interfere with the discretion of the Commissioner (Appeals) in the exercise of his appellate functions.
2. The CBDT if it considers it desirable or expedient to avoid genuine hardship in any case or class of cases, may by general or special order, authorize any income-tax authority other than Commissioner (Appeals) **to admit an application or claim** for any exemption, deduction, refund or any other relief under the Act after the expiry of the period specified by the Act for making such application or claim.
3. The CBDT may for the proper and efficient management of the work or assessment and collection of revenue, issue from time to time, general or special orders in respect of any class of income or class of cases, **setting forth procedures to be followed by income-tax authorities** in relation to assessment, collection of revenue or initiation of proceedings for penalties.
4. The CBDT may if it considers desirable or expedient so to do for avoiding genuine hardship in any case or class of cases, by general or special order relax any requirement contained in any of the provisions of Chapter IV or Chapter VI-A where the assessee has failed to comply with any requirement contained in any of the provisions for claiming deduction thereunder. This is subject to the following conditions:

- (a) CBDT shall specify the reasons for issuing such order.
- (b) The default in complying with such requirement was due to circumstances beyond the control of the assessee.
- (c) The assessee has complied with such requirement before the completion of assessment in relation to the previous year in which such deduction is claimed.

DIRECTOR GENERAL / DIRECTOR

11.3

Director General or Director, appointed by the Central Government, are required to perform such functions as may be assigned by the Central Board of Direct Taxes. The Director General / Director have the following powers under the various provisions of the Act:

1. To give instructions to the Income-tax Officers.
2. To enquire or investigate into concealment.
3. To order for and carry out search and seizure.
4. To requisite books of accounts.
5. To conduct survey.
6. To conduct any enquiry.

COMMISSIONERS OF INCOME-TAX

11.4

Commissioners of Income-tax are appointed by the Central Government. They are usually appointed to head the administration of a particular area or jurisdiction. The following are the powers enjoyed by the Commissioners of Income-tax under the Act:

1. To grant registration for Charitable Trust or Institutions.
2. To grant approval of an annuity contract.
3. To appoint Income-tax Officers and Inspectors.
4. To provide instructions to subordinate authorities.
5. To permit shifting of jurisdiction.
6. To permit transfer of cases.
7. To assign functions of Inspectors of Income-tax.
8. To demand for discovery and production of evidence.
9. To conduct search and seizure.
10. To requisite books of accounts.
11. To conduct any enquiry.
12. To disclose information respecting assessee.
13. To grant sanction for issue of notice to reopen assessment after expiry of 4 years.

14. To authorize income-tax officers to recover any arrears of tax due from an assessee by distraint and sale of his movable property.
15. To set-off refunds against tax remaining payable.
16. To direct the Assessing Officer to prefer an appeal to Appellate Tribunal against the order passed by the Assessing Officer which are prejudicial to the revenue.
17. To revise orders passed by subordinate authorities on his own motion or on the application of the assessee.
18. To reduce or waive penalty.
19. To award and withdraw recognition to Provident Funds.

COMMISSIONERS (APPEALS)

11.5

Commissioners of Income-tax (Appeals) are appointed by the Central Government. They are empowered for the following:

1. To demand discovery and production of evidence.
2. To call for information.
3. To inspect register of companies.
4. To set-off refunds against tax remaining payable.
5. To dispose of appeals.
6. To impose penalty.
7. To confirm, reduce, enhance or annul the assessment.
8. To confirm, cancel or vary an order imposing penalty.

JOINT COMMISSIONERS

11.6

They are appointed by the Central Government and are vested with the following powers and functions:

1. To detect tax evasion.
2. To supervise subordinate officers.
3. To provide instructions to the Assessing Officers.
4. To demand discovery and production of evidence.
5. To conduct search and seizure.
6. To call for information.
7. To conduct survey.
8. To inspect register of companies.
9. To make any enquiry.
10. To grant approval to the concerned assessing officer to impose penalty.

INCOME-TAX OFFICERS**11.7**

The appointment of Class I Income-tax Officers is made by the Central Government and that of Class II by the Commissioner of Income-tax. The following are the powers and functions of the Income-tax officers under the various provisions of the Act:

1. To discover and produce evidence.
2. To conduct search and seizure.
3. To requisite books of accounts.
4. To apply retained assets.
5. To call for information.
6. To conduct survey.
7. To inspect register of companies.
8. To allot Permanent Account Numbers.
9. To make assessment.
10. To impose penalties.
11. To issue directions for getting accounts audited.
12. To reassess escaped income.
13. To permit rectification of mistakes.
14. To grant approval for deduction of tax at source at lower rates of tax.
15. To demand advance payment of tax.
16. To grant refunds, etc.

INSPECTORS OF INCOME-TAX**11.8**

They are appointed by the Commissioner of Income-tax. They are required to perform such functions as assigned to them by the Commissioner or any other authority under whom they are appointed to work.

SUMMARY

- For the levy, administration and collection of direct taxes, various authorities are set up. These are called Income Tax Authorities.
- The hierarchy of Income Tax Authorities is – Central Board of Direct Taxes, Director General/Director, Commissioners of Income Tax, Commissioner (Appeals), Joint Commissioners, Income Tax Officers and Income Tax Inspectors.
- The main responsibility of the Central Board of Direct Taxes (CBDT) is to issue, from time to time, orders, directions and instructions to other authorities for proper administration.

- Director General or Director, appointed by the Central Government, are required to perform such functions as may be assigned by the Central Board of Direct Taxes. The Director General / Director have the following powers under the various provisions of the Act – to give instructions to the Income-tax Officers, to enquire or investigate into concealment, to order for and carry out search and seizure, to requisite books of accounts, to conduct survey, and to conduct any enquiry.
- Commissioners of Income-tax are appointed to head the administration of a particular area or jurisdiction. The following are the powers enjoyed by the Commissioners of Income-tax under the Act – to grant registration for Charitable Trust or Institutions, to grant approval of an annuity contract, to appoint Income-tax Officers and Inspectors, to provide instructions to subordinate authorities, to permit shifting of jurisdiction, to permit transfer of cases, to assign functions of Inspectors of Income-tax, to demand for discovery and production of evidence, to conduct search and seizure, to requisite books of accounts, to conduct any enquiry, etc.
- Commissioners of Income-tax (Appeals) are empowered for the following – to demand discovery and production of evidence, to call for information, to inspect register of companies, to set-off refunds against tax remaining payable, to dispose of appeals, to impose penalty, etc.
- Joint Commissioners are vested with the following powers and functions – to detect tax evasion, to supervise subordinate officers, to provide instructions to the Assessing Officers, to demand discovery and production of evidence, to conduct search and seizure, to call for information, etc.
- The following are the powers and functions of the income-tax officers under the various provisions of the Act – to discover and produce evidence, to conduct search and seizure, to requisite books of accounts, to apply retained assets, to call for information, to conduct survey, to inspect register of companies, to allot Permanent Account Numbers, to make assessment, to demand advance payment of tax, to grant refunds, etc.
- Inspectors of Income Tax are appointed by the Commissioner of Income-tax. They are required to perform such functions as assigned to them by the Commissioner or any other authority under whom they are appointed to work.

THEORY QUESTIONS

Section A Type Questions

1. List any four Income-tax Authorities.
2. State any two powers of the CBDT.
3. State the powers of Director General/Director.
4. List out the powers of Commissioner (Appeals).
5. Write short note on 'Income Tax Officers' and 'Inspectors of Income Tax'.

Section B Type Questions

1. List out the various Income-tax Authorities constituted under the Income-tax Act.
2. Explain the various powers of the Central Board of Direct Taxes.
3. Elucidate the various functions and powers of Commissioners of Income-tax.
4. List out the powers vested upon Joint Commissioners of Income-tax.
5. Briefly list out the various powers and functions of Income-tax Officers.

1

Model Question Paper

INCOME TAX-I
B.Com Semester-V

Time: 3 Hours

Max. Marks: 70

Section-A

1. Answer any five sub-questions. Each question carries two marks. (5 × 2 = 10 marks)
- (a) What is 'Assessment'?
 - (b) Who is a 'person' according to Income Tax Act, 1961?
 - (c) List the exceptions for the 'General Rule of Previous Year'?
 - (d) Who is a 'person of Indian origin'?
 - (e) What is an 'Indian Income'?
 - (f) Differentiate between 'revenue receipts' and 'capital receipts', from tax perspective.
 - (g) State the golden rule of Income Tax.

Section-B

Answer any **three** questions. Each question carries **six** marks. (3 × 6 = 18 marks)

- 2. Explain the chargeability under the heads—Salaries and House Property.
- 3. List the various authorities constituted under the Income Tax Act, 1961.
- 4. Mr. Ramesh, born and brought up in India, joined a company in Bahrain on 1st October, 2013. He came back to India on 25th April, 2014 and went back on 25th May, 2014. He again came to India on 25th March, 2015 and left back on 22nd May, 2015. Due to acute

M-1.2 • Income Tax - I

illness, he came back to India on leave on 15th October, 2015 and joined back his duty on 1st August, 2017. He resigned his job on 1st January, 2018 and came back to India on 1st February, 2018. Determine the residential status for the assessment year 2018-19.

(Ans: Resident and Ordinarily a Resident)

5. Srinivas, a resident of Mandya, receives ₹9,90,000 per annum as basic salary. In addition, he gets ₹2,60,000 per annum as dearness allowance, which does not form part of basic salary, 6 per cent commission on turnover achieved by him (turnover achieved by him during the relevant previous year 2017-18 is ₹80,00,000). And ₹3,00,000 per annum as house rent allowance. He, however, pays ₹2,45,000 per annum as house rent. Determine the quantum of house rent allowance exempt from tax.

(Ans: ₹98,000)

6. Calculate Gross Annual Value from the following particulars:

- (a) Monthly Rent: ₹8,500
- (b) Municipal Rent: ₹65,000
- (c) Fair Rent: ₹69,000
- (d) Standard Rent: ₹55,000

The assessee could not realize rent for one month and the house also remained vacant for three months during the Previous Year 2017-18.

(Ans: ₹68,000)

Section-C

Answer any **three** questions. Each question carries **fourteen** marks. (3 × 14 = 42 marks)

7. Explain in detail, determination of residential status of individual assesseees.
8. Amit Sen received the following emoluments during the previous year ending March 31, 2018:

Basic salary: ₹9,00,000, dearness allowance: ₹90,000 (not forming part of salary), bonus: ₹74,000 and commission: ₹40,000.

His employer provides the following perquisites:

A rent-free furnished house in Cochin:

Lease rent of unfurnished house: ₹41,000

Cost of steel furniture provided (written down value ₹12,000, steel furniture is provided throughout the previous year): ₹14,000.

Rent of furniture (rent is yet to be paid by employer): ₹17,000.

Motor car expenditure of the employee (reimbursed by employer): ₹6,000.

Determine the value of the perquisite in respect of rent-free furnished house if:

- (a) Amit Sen is an officer in the Government of West Bengal and ₹18,000 is licence fee of unfurnished house as per the State Government Rules,
 (b) Amit Sen is an Officer of the Indian Airlines, and
 (c) Amit Sen is Managing Director of a Private Company.

What will be the value of perquisite, in all the above cases, if employer charges Amit Sen a rent of ₹40,000 per annum?

(Ans: Value of Rent-free Furnished House: (a) ₹36,400, (b) ₹59,400 and (c) ₹59,400, Value of Accommodation provided at Concessional Rent: (a) Nil (b) ₹19,400 and (c) ₹19,400)

9. Mr. Shankar is the owner of three house properties in Bengaluru and has let out all the houses throughout the year.

Particulars	House A ₹	House B ₹	House C ₹
Fair Rent	1,80,000	1,50,000	1,20,000
Municipal Valuation	1,50,000	2,00,000	1,00,000
Let out (per month)	20,000	15,000	25,000
Use by tenant	Residential	Office	Residential
Repair charges	10,000	—	40,000
Collection charges	20,000	5,000	—
Interest on loan			
For construction	1,00,000	—	—
For marriage of daughter	—	60,000	—
For repairs	—	—	10,000

Municipal tax is 10% of municipal valuation. Municipal tax of house A was paid by owner but municipal tax of house B was not paid upto 31st March 2018 and municipal tax of house C was paid by tenant. The house C remained vacant for 2 months during the PY. Compute income from house property for the AY 2018-19.

(Ans: House I: ₹57,500, House II: ₹1,40,000, House III: ₹1,65,000, Total Income from House Property: ₹3,62,500)

10. Mr. Akhil, Sales Manager of XYZ Ltd., Mumbai has furnished the following details of his income for the year ended 31st March 2018. Compute his income from salary for the Assessment Year 2018-19.

- (a) Basic salary: ₹20,000 pm
 (b) Dearness allowance: ₹6,000 pm (forming part of salary)

M-1.4 • Income Tax - I

- (c) Bonus equal to 3 months basic salary
- (d) Entertainment allowance: ₹2,500pm (amount spent: ₹12,000)
- (e) Children hostel allowance for his three children ₹400 pm per child
- (f) Reimbursement of medical bills ₹22,000 for the treatment taken in a private nursing home
- (g) He is provided with rent free furnished accommodation owned by the company. Cost of furniture: ₹1,00,000. Fair Rent of the house is ₹7,500 pm.
- (h) Free telephone at his residence: ₹3,500
- (i) Medical insurance premium of Mr. Pratham paid by the company: ₹4,000 pa.
- (j) Own contribution and company's contribution to RPF is 14% of salary. Interest credited to RPF at 14% pa is ₹14,000

(Ans: ₹5,02,320)

11. Mr. Krishna furnishes the following particulars of his income earned during the Previous Year 2017–18:

- (a) Profit from business in Chennai: ₹50,000
- (b) Income from agriculture in Sri Lanka: ₹1,90,000
- (c) Income from property in Mexico received there ₹2,00,000
- (d) Interest on Singapore Development Bonds: ₹1,50,000 (1/3 received in India)
- (e) Income from business in Kuwait controlled from Mumbai: ₹85,000 (₹35,000 was received in India)
- (f) Dividend from domestic company: ₹1,000
- (g) Profit on sale of building in Bengaluru received in Nepal: ₹50,000
- (h) Income from agriculture in Punjab: ₹1,00,000
- (i) Profit on sale of plant at London: ₹50,000 (50% is received in India)
- (j) Income from house property in Nepal received in Mandya: ₹25,000
- (k) Dividends from UK based company received in UK: ₹27,000

Compute his Gross Total Income for the Assessment Year 2018–19 if he is: (a) Ordinarily Resident (b) Not ordinarily Resident and (c) Non-Resident

(Ans: (a) ₹8,27,000, (b) ₹2,85,000 and (c) ₹2,35,000)

2

Model Question Paper

INCOME TAX-I B.Com Semester V

Time: 3 Hours

Max. Marks: 70

Section-A

1. Answer any **five** sub-questions. Each question carries **two** marks. (5 × 2 = 10 marks)
- (a) Define 'Assessee' in accordance with Income Tax Act, 1961.
 - (b) List the exceptions for the 'General Rule of Previous Year'.
 - (c) What are 'Revenue Receipts'? Give examples.
 - (d) State the chargeability under the head 'Income from Salaries'.
 - (e) Write short note on 'Income Tax Officers' and 'Inspectors of Income Tax'.
 - (f) What is 'Agricultural Income'? Give three examples.
 - (g) State the conditions under Section 6(1) for determining residential status of individuals.

Section-B

Answer any **three** questions. Each question carries **six** marks. (3 × 6 = 18 marks)

- 2. What is meant by 'Canons of Taxation'? Briefly explain the various canons of taxation.
- 3. What is Incidence of Tax? Explain the consideration of foreign incomes based on residential status.
- 4. Ascertain the category of 'person' of the following assessee:
 - (a) Ms. Shashikala
 - (b) Kandala Brothers LLP

M-2.2 • Income Tax - I

- (c) BHS Higher Education Society
- (d) Center for Economic and Social Studies
- (e) Bangalore Central University
- (f) McGraw-Hill Education (India) Pvt. Ltd.
- (g) Suraj and Family.
- (h) BMRCL Employees Union
- (i) Delhi Development Authority

*(Ans: (a) Individual (b) Firm (c) BOI/AOP (d) Artificial Juridical Person
(e) Artificial Juridical Person (f) Company (g) Hindu Undivided Family
(h) BOI/AOP and (i) Local Authority)*

5. Mr. George, a foreign citizen, comes to India for the first time on 15th April 2013. During the Financial Years 2013–14; 2014–15; 2015–16; 2016–17 and 2017–18 he is in India for 130 days, 80 days, 13 days, 210 days and 75 days. Determine his residential status for Assessment Year 2018–19.

(Ans: Resident but not ordinarily resident)

6. State whether the following are agricultural or non-agricultural incomes:

- (a) Income from agricultural land situated in Australia
- (b) Income derived from sale of seeds
- (c) Income from sale of forest trees of spontaneous growth
- (d) Lease rent received from land given to tenants for agricultural operations
- (e) Income derived from land used as stone quarries
- (f) Income from sale of plants from nursery

(Ans: (a) No (b) Yes (c) No (d) Yes (e) No and (f) Yes)

Section-C

Answer any **three** questions. Each question carries **fourteen** marks. (3 × 14 = 42 marks)

7. Explain the 'chargeability' of income under various heads of income, according to the Income Tax Act, 1961.
8. Mr. Akshay furnishes the following particulars of his income for the PY 2017–18.
- (a) Income from business in Hubballi: ₹1,00,000
 - (b) Profit from business in UK controlled from India: ₹60,000
 - (c) Income from house property in Japan received there: ₹50,000
 - (d) Income from business in India received in Pakistan: ₹30,000
 - (e) Salary received in India for services rendered in USA: ₹70,000
 - (f) Interest on deposits with SBI in Mysuru: ₹20,000
 - (g) Profit from business in Singapore controlled from India (1/3 received in India): ₹30,000

- (h) Past untaxed income brought to India: ₹8,000
 (i) Dividend received from a domestic company: ₹5,000
 (j) Agricultural income earned in Nepal: ₹25,000
 (k) Commission received in India for service given in Japan: ₹10,000
 (l) Income from profession in India but received in France: ₹10,000

Determine his gross total income for the AY 2018:19 if his residential status is (a) Ordinarily Resident (b) Not Ordinarily Resident and (c) Non-Resident

(Ans: (a) ₹4,05,000, (b) ₹3,30,000 and (c) ₹2,50,000)

9. Vinay (age: 34 years) receives the following emoluments during the previous year ending 31st March 2018:

Basic pay ₹5,52,000.

Commission ₹2,60,000.

Free car facility for Vinay and his family members only for private use

(expenditure of the employer including normal wear and tear: ₹1,21,000)

Entertainment allowance ₹30,000.

On 1st October 2017, the employer gives a housing loan of ₹11,70,000 @ 2 per cent per annum (payable in 15 years) (SBI lending rate: 10.15 per cent).

Vinay contributes ₹1,60,000 towards recognised provident fund. Determine the taxable salary for Assessment Year 2018–19 if:

- (a) Vinay is an employee of VPG, a Partnership firm.
 (b) Vinay is an employee of the Punjab Government since 1984.

(Ans: (a) ₹9,63,000 and (b) ₹9,58,000)

10. Mrs. Sreevidhya owns three houses in KGF. From the following particulars compute her taxable income from house property for the Assessment Year 2018–19.

Particulars	House I ₹	House II ₹	House III ₹
Municipal Value	60,000	90,000	65,000
Fair rent	65,000	1,00,000	60,000
Rent received	—	88,000	—
Municipal tax paid at 10% of municipal value			
Repairs	1,000	8,000	6,000
Interest on loan take for house construction	—	10,000	8,000
How used	Self-occupied for Residence	Let-out	Self-occupied for Residence

M-2.4 • Income Tax - I

*(Ans: House I: ₹41,300, House II: ₹53,700, House III: ₹8,000,
Total Income from House Property: ₹87,000)*

[Hint: It is advisable for Mrs. Sreevidhya to consider House I as
Self-occupied Property for Assessment purposes)

11. Mrs. Smitha is working as Sales Executive in Maruthi Suzuki Ltd., Kolkata and her salary details are as follows for the Previous Year 2017–18

- (a) Basic salary: ₹21,000 pm
- (b) Bonus equal to two months' basic salary
- (c) Commission at 3% on sales (During the year she has reached sales target of ₹5,00,000)
- (d) Dearness Allowance: ₹7,000 pm (eligible for retirement benefits)
- (e) Medical allowance: ₹1,400 pm (Medical expenses ₹15,000 pa)
- (f) Children Hostel Allowance for her two children at ₹500 pm per child
- (g) Children Education Allowance for her two children at ₹400 pm per child
- (h) RPF contribution by the company: ₹6,000 pm
- (i) RPF contribution by the employee: ₹5,000 pm
- (j) Interest credited on RPF at 11% ₹44,000
- (k) She has been provided with company's owned rent free furnished house in Kolkata and cost of furniture provided is ₹60,000
- (l) Mrs. Smitha has paid her professional tax ₹2,400 pa

Compute Taxable Salary for the Assessment Year 2018-19.

(Ans: ₹5,24,550)

3

Model Question Paper

INCOME TAX-I
B.Com Semester V

Time: 3 Hours

Max. Marks: 70

Section-A

1. Answer any **five** sub-questions. Each question carries **two** marks. (5 × 2 = 10 marks)
- (a) What is 'Tax'? State the differences between Direct Tax and Indirect Tax.
 - (b) What is the Previous Year for a business or professions newly set up or for a new source of income?
 - (c) When is an individual assessee considered as 'Resident, but not ordinarily a resident'?
 - (d) What are the criteria for classifying incomes into 'Indian Incomes' and 'Foreign Incomes'?
 - (e) List any six incomes which are exempt from tax.
 - (f) State the chargeability for 'Income from House Property'.
 - (g) State any four powers of the CBDT.

Section-B

Answer any **three** questions. Each question carries **six** marks. (3 × 6 = 18 marks)

- 2. Define 'Person' according to Income Tax Act, 1961 and explain the meaning and inclusion of each category, with examples.
- 3. List the conditions under Section 6(1) and 6(6) applicable for determining residential status. Also list out the exceptions for the condition under Section 6(1)(b).

M-3.2 • Income Tax - I

4. Classify the following incomes into Revenue Receipts and Capital Receipts
- (a) Compensation received for termination of contract by Supplier of Raw materials.
 - (b) Amount received on maturity of Life Insurance Policy.
 - (c) Accumulated balance of Provident Fund withdrawn.
 - (d) Interest on Savings Bank Account credited to the Account.
 - (e) Amount received on maturity of Fixed Deposit.
 - (f) Dividend income from Google Inc.
 - (g) Amount received on sale of shares of Bharat Dynamics Ltd.
- (Ans: (a) Capital (b) Capital (c) Capital (d) Revenue (e) Capital (f) Revenue (g) Capital)*
5. Mr. Veeresh, a citizen of England came to India for the first time on 1/5/2011. He stayed in India without any break for 3 years and left for Singapore on 1/5/2014. He returned to India on 1/4/2015 and went back to England on 1/12/2015. He was pointed back to India on 20/1/2018. Determine his residential status for the Assessment Year 2018-19
- (Ans: Resident and ordinarily a resident)*
6. Mr. Vinodh retired from services on 31st March 2017. His pension was fixed at ₹16,000 per month. He commutes 3/4th of his pension and receives ₹14,40,000 during the Previous Year 2017–18. Find out the taxable amount of commuted pension when:
- (a) He is Government Employee
 - (b) He is not a Government Employee but is receiving Gratuity
 - (c) He is not a Government Employee and is not receiving Gratuity
- (Ans: (a) ₹Nil; (b) ₹8,00,000 & (c) ₹4,80,000)*

Section-C

Answer any **three** questions. Each question carries **fourteen** marks. (3 × 14 = 42 marks)

7. Explain in detail the provisions for valuation of 'rent-free accommodation'.
8. Following are the incomes of Mr. Vishnu for the Previous Year 2017–18:
- (a) Received ₹20,000 in India, which accrued in England
 - (b) ₹10,000 earned in India but received in England
 - (c) ₹5,000 were earned and received in Africa but brought to India
 - (d) ₹10,000 were earned and received in Japan from a business which was controlled and managed in Japan
 - (e) ₹16,000 was untaxed foreign income of some earlier year, which was brought to India in the PY
 - (f) Interest on fixed deposit in SBI, Bengaluru: ₹1,200
 - (g) Income from agriculture in Africa: ₹10,000
 - (h) Dividends received in UK from an American Company: ₹10,000

- (i) Salary income for three months for working in Indian Embassy's office in Australia and salary received there ₹72,000
- (j) Income from house property in Mumbai: ₹1,00,000
- (k) Interest received on Post Office Savings Bank A/c: ₹1,000
- (l) Pension income from Belgium for services rendered in India with a limited company: ₹20,000
- (m) Gift from relatives: ₹80,000

What is the Gross Total Income of Mr. Vishnu if he is (a) a Resident and Ordinarily Resident (b) a Resident but not Ordinarily Resident and (c) a Non-Resident?

(Ans: (a) ₹2,58,200, (b) ₹2,23,200 and (c) ₹2,23,200)

[Hint:

- (i) Unless specifically mentioned, income is assumed to be received in the place of accrual.
- (ii) Past untaxed income brought into India is not taxable.
- (iii) Salary income for working in Indian Embassy's Office outside India is 'deemed to accrue in India' and hence is taxable in the hands of the assessee irrespective of the residential status.
- (iv) Interest on Post Office Savings Bank Account is exempt from tax u/s 10(15)
- (v) Gift from relatives is exempt from tax u/s 56(2).]

9. Mr. Pramod is an employee of PQR Ltd., Chennai. He draws Basic Salary: ₹2,00,000; Dearness Allowance: ₹15,000; Bonus: ₹20,000 and Children Education Allowance: ₹3,600 (for the education of his daughter) during the Previous Year 2017-18. Besides the above, the company provides him a residential accommodation free of rent. You are required to calculate the taxable value of rent free accommodation for the Assessment Year 2018-19 if the house is:

- (a) Owned by the company
- (b) Leased by the company at a lease rent of ₹20,000 per annum

(Nov/Dec 2010 – Modified)

(Ans: (a) ₹33,360 & (b) ₹20,000)

10. Mr. Harish resides in Mumbai. During the Previous Year 2017-18 he gets Basic Salary: ₹12,000 per month, Dearness Allowance: 20%, Medical Allowance: ₹300 per month and Special Allowance: ₹250 per month. He is provided with a rent-free accommodation. The cost of furniture provided is ₹1,20,000. You are required to compute taxable value of rent free furnished accommodation for the Assessment Year 2018-19.

(Ans: ₹34,590)

M-3.4 • Income Tax - I

11. Mr. Suryakantha has three houses in Mandya and particulars of which are relating to the Previous Year 2017–18 are as under:

Particulars	House I ₹	House II ₹	House III ₹
Use of house	Let out	Let out	Self-occupied
Standard Rent	1,50,000	2,00,000	–
Municipal Value	1,00,000	3,00,000	3,00,000
Fair Rental Value	1,80,000	1,80,000	3,50,000
Actual rent per month	15,000	20,000	–
Municipal tax paid	10%	10%	10%
Repair charges	–	–	2,000

Suryakantha borrows ₹6,00,000 at 10% per annum from the bank for construction of house III (date of borrowing 1/6/2013 and date of repayment of entire amount of loan together with interest 30/9/2017). Construction of the house is completed in June 2016. Determine the taxable income from house property for the Assessment Year 2018–19.

(Ans: House I: ₹1,19,000, House II: ₹1,47,000, House III: ₹64,000, Total Income from House Property: ₹2,02,000)

12. Sri Krishna, an employee of a Transport Company, Bengaluru submits the following information relevant for the Assessment Year 2018–19:

- Basic salary: ₹8,000 pm
 - Conveyance allowance (60% spent for official purpose): ₹2,000 pm
 - City compensatory allowance: ₹300 pm
 - Bonus: ₹10,000 pa
 - DA: ₹1,500 pm (does not form part of salary)
 - HRA: ₹5,000 pm (Rent paid ₹7,000 pm)
 - Payment of LIC premium by the company: ₹4,000 pa
 - Services of sweeper paid by the company: ₹200 pm
 - Leave travel concession: ₹10,000 (first time in the current block period)
 - Reimbursement of gas, electricity and water bill by the company: ₹2,500 pa
 - Own contribution and company's contribution to the RPF is 14% of salary
 - Interest credited to RPF at 14%: ₹14,000
 - Gift worth ₹10,000 during festival season received from the company during the PY
- Compute his taxable income from salary.

(Ans: ₹1,79,120)