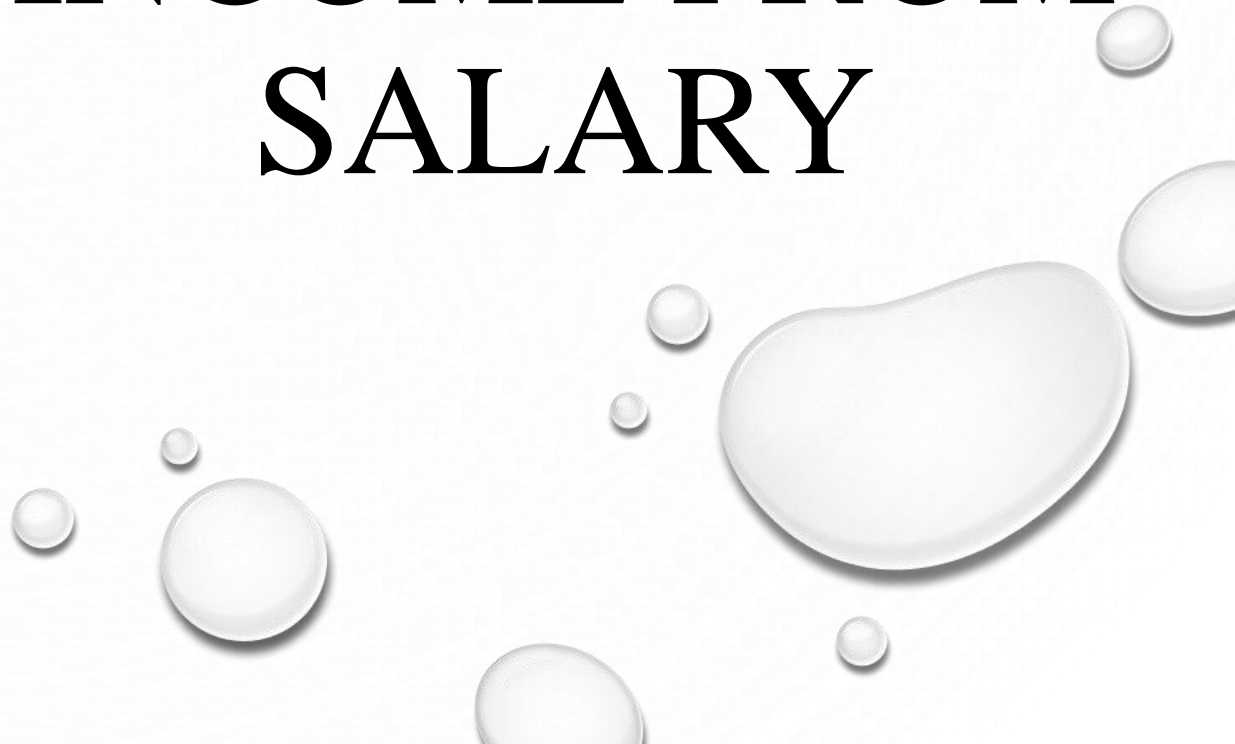


INCOME FROM SALARY



INTRODUCTION

- ❖ Salary is income generated from an **Employer – Employee** relationship

- ❖ The word “Salary” according to Section 17(1) includes –
 1. Wages
 2. Any annuity or pension
 3. Any gratuity
 4. Any fees, perquisites or profits in lieu of salary
 5. Advance salary
 6. Leave Encashment

CHARGING SECTION 15

- ❖ Following incomes are chargeable to Income Tax under the head “Salaries” -
1. Any salary **DUE** to the assessee from an employer or a former employer in the P.Y. whether paid or not.
 2. Any salary **PAID or ALLOWED** to the assessee from an employer or former employer in the P.Y. whether due to be paid or not.
 3. Any **ARREARS** of salary paid to assessee and not charged under Income Tax in any of the past Previous years

BASIC CLASSIFICATION OF SALARIES

❖ “Salaries” can be divided in 4 basic parts -

1. Normal / Regular Salary

2. Allowances

3. Perquisites

4. Retirement Benefits

NORMAL / REGULAR SALARY

❖ Following is included in the normal salary -

1. Basic Salary
2. Dearness Allowance
3. Commission
4. Bonus

ALLOWANCES

- ❖ Allowances are fixed monetary amounts paid by the employer to the employee
- ❖ These expenses can be personal or for the performance of particular duties.
- ❖ These allowances are generally taxable unless a specific exemption is provided
- ❖ Most importantly, these allowances are paid irrespective of the requirement of such an allowance

PERQUISITES

- ❖ These are casual benefits or emoluments attached to a particular office position in addition to salary or wages
- ❖ Such perquisites can be in Cash or in Kind
- ❖ These are generally not paid on a regular basis
- ❖ Examples – Accommodation , Reimbursements, Motor cars etc..

RETIREMENT BENEFITS

❖ These are benefits received by the employee at the time of Retirement or when he/she leaves that particular organization or at the time the employee's death

❖ Examples –

Provident Fund

Gratuity

Leave Encashment

Pension

PROVIDENT FUNDS

<u>Particulars</u>	<u>Statutory PF</u>	<u>Recognized PF</u>	<u>Unrecognized PF</u>	<u>Public PF</u>
<u>Employer's Contribution</u>	Exempt	Exempt upto 12% of salary	Exempt	Not Applicable
<u>Interest Credited</u>	Exempt	Exempt upto 9.5%	Exempt	Exempt
<u>Lump sum payment at the time of Retirement</u>	Exempt	Exempt	Special Calculation	Exempt

DEDUCTIONS

- ❖ There are a 3 “Salary specific” Deductions which are covered under Sec. 16

- ❖ They are –
 1. Standard deduction – [Sec. 16 (i)]

 2. Entertainment Allowance – [Sec. 16 (ii)]

 3. Professional tax – [Sec. 16 (iii)]

COMPUTATION OF SALARY

PARTICULARS	Rs.	Rs.
NORMAL SALARY		
TAXABLE ALLOWANCES		
TAXABLE RETIREMENT BENEFITS		
TAXABLE PERQUISITES		
CONTRIBUTION and INTEREST TO RPF		
<u>GROSS SALARY</u>		
Less - DEDUCTIONS		
<u>INCOME CHARGEABLE TO SALARIES</u>		

TAXABILITY OF VARIOUS COMPONENTS OF SALARY

ALLOWANCES

- ❖ Allowances are fixed monetary amounts paid by the employer to the employee
- ❖ These expenses can be personal or for the performance of particular duties.
- ❖ These allowances are generally taxable unless a specific exemption is provided
- ❖ Most importantly, these allowances are paid irrespective of the requirement of such an allowance

FULLY EXEMPT ALLOWANCES

1. Allowances given to High court and Supreme court judges
2. Allowances paid by the United Nations Organisation
3. Compensatory Allowance paid to any judge
4. Allowances given to Government employees working outside India

FULLY TAXABLE ALLOWANCES

- ❖ Before the advent of standard deduction there were many partially exempt allowances
- ❖ However now, most of the allowances are fully taxable. Few examples are -
 1. Entertainment Allowance*
 2. Fixed Medical Allowance
 3. City Compensatory Allowance
 4. Tiffin / Meal Allowance
 5. Transport Allowance (other than blind / deaf & dumb / orthopedically handicapped)
 6. Non – Practicing Allowance

PARTIALLY EXEMPT ALLOWANCES

ALLOWANCES WITH A PRESCRIBED MONETARY LIMIT

ALLOWANCE	EXEMPTION
Special Compensatory Allowance (Hilly Areas)	<ul style="list-style-type: none">• Rs. 800/- or Rs. 300/- per month based on location• Rs. 7,000/- per month for “Siachen” area
Special Compensatory Allowance (Tribal / scheduled areas)	<ul style="list-style-type: none">• Rs. 200/- per month
Children Education Allowance	<ul style="list-style-type: none">• Rs. 100/- per month per child up to <u>2</u> children
Children Hostel Allowance	<ul style="list-style-type: none">• Rs. 300/- per month per child up to <u>2</u> children
Transport Allowance to blind / deaf & dumb and orthopedically handicapped	<ul style="list-style-type: none">• Rs. 3,200/- per month

PARTIALLY EXEMPT ALLOWANCES

ALLOWANCES EXEMPT UP TO AMOUNT SPENT

ALLOWANCE
Travelling / Conveyance Allowance for cost of travel on tour / transfer
Daily Allowance
Helper Allowance
Research Allowance
Uniform Allowance

HOUSE RENT ALLOWANCE (HRA)

❖ Special Allowance paid towards the rent for residence of the employee

HRA is exempt to the extent of least of the following 3 conditions

- 1.) HRA actually **received** for the relevant period
- 2.) **Rent paid** (-) **10%** of the salary for the relevant period
- 3.) **50%** salary (For metro cities – **Mumbai, Kolkata, Chennai and Delhi**)
OR
40% salary (For other cities)

Salary = Basic + D.A + Commission as a % on turnover

Relevant period = The period for which the assessee occupied that property

Let us understand HRA through an example

Mr. A, the assessee, gives you the following details for P.Y. 2019-20

Particulars	Amount (Rs.)
Basic Pay	Rs. 3,000/- per month
Dearness Allowance	Rs. 600/- per month
Commission	Rs. 6,000/- per year
Motor car expenditure paid by employer	Rs. 500/- per month
House Rent Allowance Received	Rs. 900/- per month
Rent actually paid by Mr. A for accommodation at Kanpur	Rs. 1,000/- per month

Find the amount of HRA taxable in the hands of Mr. A

Exemption for H.R.A -

HRA is exempt to the extent of <u>LOWEST</u> of the following <u>3</u> conditions		
1.) HRA actually received	(900×12)	Rs. 10,800/-
2.) Rent paid (-) 10% of the salary	$(1000 \times 12) - (10\% \text{ of } 3600 \times 12)$	Rs. 7,680/-
3.) 40% salary (For other cities)	$(3600 \times 12) \times 40\%$	Rs. 17,280/-

Salary = Basic + D.A.

Hence, Salary = 3,000 + 600 = **Rs. 3,600/-** per month

COMPUTATION OF TAXABLE HOUSE RENT ALLOWANCE (HRA)

<u>Particulars</u>	<u>Amount (Rs.)</u>
HRA Actually received	10,800
(Less) – HRA exempt	(7,680)
<u>Taxable HRA</u>	<u>3,120/-</u>

RETIREMENT BENEFITS

❖ These are benefits received by the employee at the time of Retirement or when he/she leaves that particular organization or at the time the employee's death

❖ Examples –

Provident Fund

Gratuity

Leave Encashment

Pension

GRATUITY

- ❖ Gratuity is a voluntary payment made by an employer for an employee's services.
- ❖ This Gratuity has nowadays become a normal payment.
- ❖ Payment of Gratuity Act, 1972 (POGA) is a statutory recognition of Gratuity.
- ❖ Generally, Gratuity is paid at the time of termination, retirement, death or permanent incapacitation of the employee.

TAXABILITY OF GRATUITY

❖ Fully Taxable

Gratuity paid to an employee during their service is fully taxable.

❖ Fully Exempted

1. Retirement Gratuity received by the members of Defence services.
 2. Retirement Gratuity received by employees of Central Government, members of Civil services and employees of Local Authorities.
- ❖ There are special calculations for other employees.

GRATUITY EXEMPTION

❖ Exemption for employees covered under the Payment of Gratuity Act, 1972

Gratuity is exempt to the extent of least of the following 3 conditions

1.) Gratuity actually **received** for the relevant period

2.) **Rs. 20,00,000/-**

3.) **15 days' salary**

$$\frac{15 \times \text{Last drawn salary} \times \text{No. of years of service}}{26}$$

26

Salary = Basic + D.A.

Years of Service = Completed years or part in excess of 6 months

GRATUITY EXEMPTION

❖ Exemption for employees NOT covered under the Payment of Gratuity Act, 1972

Gratuity is exempt to the extent of least of the following 3 conditions

1.) Gratuity actually **received** for the relevant period

2.) **Rs. 10,00,000/-**

3.) **Half month's salary**

$$\frac{1 \times 10 \text{ months' Average salary} \times \text{No. of completed years of service}}{2}$$

Salary = Basic + D.A. (only for retirement benefits) + Commission (% of turnover)

Years of Service = Completed years

Let us understand Gratuity through an example

Mr. Ravi retired on 15/6/19 after a completion of 26 years and 8 months of service and received a Gratuity of Rs. 6,00,000/- He had the following incomes at the time of his retirement -

Particulars	Amount (Rs.)
Basic Pay	Rs. 5,000/- per month
Dearness Allowance (60% for retirement benefits)	Rs. 3,000/- per month
Commission @ 1% of turnover Turnover →	Rs. 12,00,000/-
Bonus	Rs. 12,000/- per year
House Rent Allowance Received	Rs. 900/- per month
Travelling Allowance	Rs. 1,000/- per month

Compute his taxable gratuity assuming -

- a) Employee covered under POGA, 1972
- b) Employee NOT covered under POGA, 1972

❖ Covered under the Payment of Gratuity Act, 1972

Gratuity is exempt to the extent of least of the following 3 conditions

1.) Gratuity actually received for the relevant period	Rs. 6,00,000/-
2.) Rs. 20,00,000/-	Rs. 20,00,000/-
3.) 15 days' salary $\frac{15 \times \text{Last drawn salary} \times \text{No. of Years of service}}{26}$ <p>(15/26 X 8,000 X 27 years)</p>	Rs. 1,24,615/-

Salary = Basic + D.A. → 5,000 + 3,000 = Rs. 8,000/-

Years of Service = Completed years or part in excess of 6 months

❖ NOT covered under the Payment of Gratuity Act, 1972

Gratuity is exempt to the extent of least of the following 3 conditions

1.) Gratuity actually received for the relevant period	Rs. 6,00,000/-
2.) Rs. 10,00,000/-	Rs. 10,00,000/-
3.) Half month's salary $\frac{1 \times 10 \text{ months' Average salary} \times \text{No. of completed years}}{2}$ (1/2 X 7,800 X 26years)	Rs. 1,01,400/-

Salary = Basic + D.A. (only for retirement benefits) + Commission (% of turnover)

$$[(5,000 \times 10) + (3,000 \times 60\% \times 10) + (1\% \times 12,00,000 \times 10/12)] \div 10 = \text{Rs. 7,800/-}$$

Years of Service = Completed years

PENSION

- ❖ Pension is a monthly payment earned by the employee post retirement until death.
- ❖ However, an ex-employee might opt to receive an amount of pension in Lumpsum
- ❖ Such pension received in Advance (lumpsum) is called “Commuted pension”
- ❖ The pension that we receive every month is called “Uncommuted Pension”

TAXABILITY OF PENSION

❖ Fully Taxable

Uncommuted Pension paid to an ex - employee is fully taxable.

❖ Fully Exempted

1. Commuted pension received by the members of Defence services.
 2. Commuted pension received by employees of Central Government, members of Civil services and employees of Local Authorities.
- ❖ There are special calculations for Commuted pension of other employees.

COMMUTED PENSION - EXEMPTION

If PENSION is Received WITH GRATUITY

1/3rd of the Amount of Pension that would be received assuming 100% pension is commuted

$$\frac{1}{3} \times 100\% \text{ Commuted Pension}$$

If PENSION is Received WITHOUT GRATUITY

Half of the Amount of Pension that would be received assuming 100% pension is commuted

$$\frac{1}{2} \times 100\% \text{ Commuted Pension}$$

Let us understand Pension through an example

Mr. R retired on 30/6/19. He had joined the company on 4/1/1986. He gets a pension of Rs. 2,000/- p.m. up to 30/11/19. On 1st Dec. he requests for commutation of 60% of his pension and receives Rs. 90,000.

Compute his taxable Pension assuming –

- a) He received a Gratuity of Rs. 50,000/-
- b) He DID NOT receive any Gratuity

GRATUITY RECEIVED – Rs. 50,000/-

PARTICULARS	RS.	RS.
Uncommuted Pension $\{(2,000 \times 5) + (800 \times 4)\}$		13,200
Commuted Pension Pension Received (60%)	90,000	
Less – Exemption (With Gratuity) ($1/3 \times 100\%$ Commuted Pension)	(50,000)	40,000
TAXABLE PENSION		<u>53,200</u>

60% Commuted Pension = Rs. 90,000/-

So,

100% Commuted Pension = Rs. 1,50,000/-

100% Uncommuted Pension = Rs. 2,000/-

So,

40% Uncommuted Pension = Rs. 800/-

GRATUITY NOT RECEIVED

PARTICULARS	RS.	RS.
Uncommuted Pension $\{(2,000 \times 5) + (800 \times 4)\}$		13,200
Commuted Pension Pension Received (60%)	90,000	
Less – Exemption (Without Gratuity) ($1/2 \times 100\%$ Commuted Pension)	(75,000)	15,000
TAXABLE PENSION		<u>28,200</u>

60% Commuted Pension = Rs. 90,000/-

So,

100% Commuted Pension = Rs. 1,50,000/-

100% Uncommuted Pension = Rs. 2,000/-

So,

40% Uncommuted Pension = Rs. 800/-

LEAVE ENCASHMENT

- ❖ As per labour law every employee is entitled to a minimum paid leaves per year.
- ❖ However, an employee might not use all these leaves.
- ❖ Such unused leaves get accumulated over a period of time.
- ❖ The employer compensates for these leaves which is called as “Leave Encashment”

TAXABILITY OF LEAVE ENCASHMENT

❖ Fully Taxable

Leave Encashment done during the service by any Employee is fully taxable.

❖ Fully Exempted

1. Retirement Encashment received by the legal heirs of a **Deceased Employee.**
 2. Retirement Encashment received by employees of **Central Government,** members of **Civil services** and employees of **Local Authorities.**
- ❖ There are special calculations for Retirement Encashment of other employees.

LEAVE ENCASHMENT

❖ Retirement Encashment for Non Government Employees

Leave Encashment is exempt to the extent of least of the following 4 conditions

- 1.) Leave Encashment actually **received**
- 2.) Statutory Amount – **Rs. 3,00,000/-**
- 3.) **Last 10 month's Salary**
- 4.) **Cash Equivalent** to the leaves due to the employee **(Max. 30 days in a year)**

Salary = Basic + D.A (for retirement benefits) + Commission as a % on turnover

Let us understand Leave Encashment through an example

Mr. Gupta retired on 1/12/19 after a completion of 20 years and 10 months of service and received a Leave Salary of Rs. 5,00,000/- Following are the incomes at the time of his retirement -

Particulars	Amount (Rs.)
Basic Pay (Rs. 1,000 p.m. was increased on 1/4/2019)	Rs. 5,000/- per month
Dearness Allowance (60% for retirement benefits)	Rs. 3,000/- per month
Commission (Fixed)	Rs. 500 p.m.
Bonus	Rs. 1,000/- p.m.
Leave availed during service	480 days
Leave entitlement per year	30 days

Compute his taxable Leave Salary assuming -

- a) He is a Government Employee
- b) He is a Non – Government Employee

LEAVE ENCASHMENT

❖ Retirement Encashment for Non Government Employees

Leave Encashment is exempt to the extent of least of the following 4 conditions

1.) Leave Encashment actually received	5,00,000
2.) Statutory Amount	3,00,000
3.) Last 10 month's Salary – [(5,000 X 8) + (4,000 X 2)] + (60% X 3,000 X 10)	66,000
4.) Cash Equivalent to the leaves – (120 / 30 X 6,600)	26,400

Salary = Basic + D.A + Commission as a % on turnover

Monthly salary = 66,000 / 10 = Rs. 6,600/-

Leaves due = (30 X 20) – 480 = 120

PERQUISITES

- ❖ These are casual benefits or emoluments attached to a particular office position in addition to salary or wages
- ❖ Such perquisites can be in Cash or in Kind
- ❖ These are generally not paid on a regular basis
- ❖ Examples – Accommodation , Reimbursements, Motor cars etc..

FULLY EXEMPT PERQUISITES

1. Telephone provided by the Employer
2. Tickets and Passes given to Indian Railways' Employees
3. Perquisites paid to employees outside of India by the Government of India
4. Employer's Contribution to staff group insurance scheme
5. Refreshments or Subsidized lunch provided by the Employer
6. **Medical Facilities**
7. Leave Travel Concession

MEDICAL FACILITIES (EXEMPT)

1. Value of medical treatment in a hospital maintained by the employer
2. Reimbursement for treatment in Government hospital
3. Reimbursement for treatment of Prescribed diseases in any hospital
4. Health insurance premium paid or reimbursed by the employer
5. Amount paid towards medical treatment outside of India

FULLY TAXABLE PERQUISITES

1. Rent Free Accommodation or Concession on Rent
2. Employees Obligation paid by the Employer
3. Life Insurance premium of the Employee paid by the Employer
4. Sweat Equity shares allotted or transferred to the Employee
5. Motor Car provided by the Employer to the Employee

EMPLOYER'S CONTRIBUTION TO R.P.F

1. The employer also contributes an equal amount as the employee in a P.F.
2. If the Employer contributes more than **12%** of the salary of the employee, then such additional amount will be taxable in the hands of the employee.
3. Salary for this purpose

Basic + D.A. (Retirement Benefits) + Commission (% on Turnover)

DEDUCTIONS

- A. Standard deduction – Rs. 50,000/- OR Gross Taxable Salary (Whichever lower)

- B. Entertainment Allowance – Only for Govt. Employees (Least of the following)
 - 1. Entertainment Allowance actually received
 - 2. Rs. 5,000/-
 - 3. $1/5^{\text{th}}$ of the Basic Salary

- C. Professional tax paid by the employee

COMPUTATION OF SALARY

PARTICULARS	Rs.	Rs.
NORMAL SALARY		
TAXABLE ALLOWANCES		
TAXABLE RETIREMENT BENEFITS		
TAXABLE PERQUISITES		
CONTRIBUTION and INTEREST TO RPF		
<u>GROSS SALARY</u>		
Less - DEDUCTIONS		
<u>INCOME CHARGEABLE TO SALARIES</u>		