



WIRC

Relearn Series Income Tax

Practical Issues in IT Return – Salary

CA Chintan Vasani

Table of Content

- Basic Concepts – Salary
- Taxation of Salary
- House Rent Allowance (Exemption)
- Case Laws on HRA Exemption
- Disclosure of Salary in Return of Income
- Employee Stock Option Plan (ESOP)
- Taxation of ESOPs
- ESOP – Disclosure requirements (including FA Schedule)
- Recent Developments
- Form 16

Relearn Series Income Tax

“Salary” - Basic Concepts

Introduction

- The Income Tax Act 1961, serves as a legal framework for imposition of income tax on various persons (including individuals) and each of those persons are subject to separate tax levies as regulated by Income Tax Act.
- Income Tax Act 1961 contains various chapters and Chapter IV prescribes income of a person under different heads of income. The Income is first assessed under the specific head of income and then tax is levied.
- Income earned under the head “Salary” holds paramount significance and this head of income encompasses the earnings received by an individual from his employment.
- Salary indicates a fixed amount or compensation paid to an employee by the employer for the work done by him for a given period of time.
- Employer – Employee / Master – Servant relationship is an essential part.

Income Tax - “Salary”

Basic Concepts

What is Salary?

- Understanding the basic provisions and its implications is crucial for both the taxpayers and authorities so as to comply effectively and ensuring a fair assessment.
- **Charging Section - Section 15** of the Act:
 - Any salary due from employer or former employer
 - Any salary paid or allowed by or on behalf of employer or a former employer
 - Any arrears paid
- Salary includes “Pension”, however excludes “Family Pension”

Income Tax - “Salary”

Basic Concepts

Some Important points:

- When salary is paid in advance and is included in total income of previous year, the same is to be excluded when it becomes due, to avoid double taxation.
- **Employer – Employee relationship:**

[Dharangadhara Chemical Works Ltd vs. State of Saurashtra 1957 SCR 152]

- Hon’ble Court held that the prima facie test of relationship is the existence of master’s right to supervise and control work of his servant.
- The test which uniformly applied in order to determine the relationship is the existence of a right to control in respect of the manner in which work is to be done.

Income Tax - “Salary”

Basic Concepts

[**Simmons vs. Health Laundry Company**]

- The Court held that Greater amount of control of power would be there if there is an existence of service contract. If there is greater independence then higher chances that it is tilted towards professional service
- Difference between “**Contract of Service**” and “**Contract for Service**” was well explained by Fletcher Moulton, “In my opinion it is impossible to lay down any rule of law distinguishing the one from the other. It is a question of fact to be decided by all the circumstances of the case. The greater the amount of direct control exercised over the person contracting for them the stronger the ground for holding it to be a Contract of Service, and similarly the greater the degree of independence of such control the greater the probability that the services rendered are of professional nature”.

[**CIT vs. Govindaswaminathan 233 ITR 264**] it was held that there is no employer – employee relation between State Govt. and Advocate General

Income Tax - “Salary”

Basic Concepts

[Justice Deoki Nanda Agarwala vs. Union of India 237 ITR 872 (SC)]

- Hon’ble Court held that the judges of the High Court and Supreme Court are not employees and has no employer, however the ipso facto does not mean that they do not receive salary.
- They are a Constitutional functionaries and Article 125 and 221 of the Constitution deals with the salaries of Supreme Court and High Court judges and specifically states that what the judge receives are to be taxed as Salary.

Income Tax - “Salary”

Basic Concepts

Salary also includes “Gratuity”

- Gratuity is understood as a payment made by the employer or former employer to the employee for the services rendered by him to the employer during his tenure.
- Gratuity Amount received during employment period is taxable under the head “Salary”
- Gratuity received by employee of CG, SG or local authority is full exempt u/s 10(10) of the Act.
- Gratuity Amount received on retirement or death is exempt u/s 10(10) of the Act subject to certain conditions as prescribed under Payment of Gratuity Act 1972.

Income Tax - “Salary”

Basic Concepts

Section 17(2) - What does Perquisites include?

- Value of rent free accommodation
- Value of any concession provided in rental accommodation
- Value of any benefit or amenity granted free of cost or at a very nominal concessional rate
- Any sum paid by employer in respect of any obligation
- Value of any specified security or sweat equity shares
- Contribution made by employer – in recognised provident fund, superannuation fund, Pension scheme of Government – To the extent it exceeds Rs. 750,000/-
- Family Allowance, Membership of a Club
- Personal Accident Policy – Premium paid by an employer **is not a perquisite.**

Income Tax - “Salary”

Basic Concepts

Section 17(3) - What is Profit in lieu of Salary?

- Any compensation due to or received by an assessee from his employer or former employer or in connection with termination of his employment or certain modifications in terms of his employment.
- Any amount due or received whether in lump sum or otherwise from any person:
 - before his joining any employment with that person; or
 - after cessation of his employment with that person.

Income Tax - “Salary” Taxation

Changes in tax rates:

Old taxation regime:

Income level (Age below 60yrs)	Income level (Age above 60yrs)	Tax Rates
Up to INR 250,000	Up to INR 300,000	Nil
INR 250,001 – INR 500,000	INR 300,001 – INR 500,000	5%
INR 500,001 – INR 1000,000	INR 500,001 – INR 500,000	20%
Above 10,00,001	Above 10,00,001	30%

Income Tax - “Salary” Taxation

Changes in tax rates:

New taxation regime: Tax u/s 115BAC

Income level	Tax Rates
Up to INR 250,000	Nil
INR 250,001 – INR 500,000	5%
INR 500,001 – INR 750,000	10%
INR 750,001 – INR 10,00,000	15%
INR 10,00,001 – INR 12,50,000	20%
INR 12,50,001 – INR 15,00,000	25%
Above INR 15,00,000	30%

Income Tax - “Salary” Taxation

New Tax Regime:

- Under new tax regime, tax rates are reduced, however certain deductions, exemptions, set off are not permitted.
- The recent Finance Act 2023, has made new tax regime as default regime i.e. applicable from AY 2024-25 onwards, unlike in current situation. The assessee has an option to Opt Out and choose old tax regime.

(AY 2024-25 onwards)

- New tax regime was first introduced in Finance Act 2020 where the assessee was given an option to choose new tax regime which offers reduced tax rates, however with certain terms and conditions.

(AY 2021-22 – AY 2023-24)

Income Tax - “Salary” Taxation

Exemptions / Deductions which are not allowed under New Tax Regime – Head “Salary”

- Leave Travel Allowance u/s 10(5)
- House Rent Allowance u/s 10(13A)
- Certain specific special allowance u/s 10(14)
- Standard Deduction Rs. 50,000/- (allowed from AY 2024-25 onwards)
- Entertainment Allowance received from Government
- Daily Allowance to member of parliament
- Chapter VI-A deductions – other than those specifically mentioned and allowed

Income Tax - “Salary” Taxation

Concessional rate of tax, conditions attached:

- Option to be exercised on or before filing return of income u/s 139(1) of the Act.
- No exemptions or deductions allowed (except few).
- Inform your deductor (i.e. employer) about your intention to opt for new taxation regime so as to allow him to deduct tax accordingly.
- Please ensure to file **Form 10-IE** (not having business income)
- If its filed in previous year, mention **Acknowledgement No and date of filing.**

Income Tax - “Salary” Taxation

Salary from more than one employer

- When an individual is working under more than one or has changed his employment.
- The employer usually deducts tax at source as per the provisions prescribed.
- The employee needs to inform his chosen or present employer details of the other employment or former employment in **writing**.
- The chosen employer or present employer as the case may be needs to deduct tax at source on aggregate amount of tax

Income Tax - “Salary” Taxation

Tax Deduction filing statement of return – Form 24Q

Certain essential points which needs to be kept in mind while filing Statement of return in Form 24Q:

- The employer should quote the gross amount (including amount exempt u/s 10 and deductions under chapter VI-A)
- The reasons for non-deduction or lower deduction or higher deduction (non-furnishing of PAN) has to be reported
- PAN of landlord shall be mentioned in case of HRA exemption
- PAN of lender shall be mandatorily furnished where the housing loan on which interest is paid is taken from a person other than financial institution or the employer.

Income Tax - “Salary” Taxation

Reporting of Perquisites:

- The person responsible for paying income which is chargeable under the head “Salary” shall be required to provide complete details of perquisites or profit in lieu of salary to the employee.
- The said details is to be furnished in Form 12BA and such form is to be furnished in addition to Form 16.

Income Tax - “Salary”

HRA Exemption

House Rent Allowance

- Any special allowance specifically granted to an assessee by his employer to meet expenditure incurred on payment of rent in respect of residential accommodation occupied by the assessee is exempt from tax.
- It is to be noted that expenditure actually incurred on payment of rent in respect of residential accommodation occupied by the assessee subject to the limits, qualify for the exemption.
- An employee has to submit details of house rent allowance to employer in Form 12BB along with rent paid receipts.
- PAN of landlord shall be mandatorily furnished where the aggregate rent paid during the previous year exceeds Rs. 100,000/-

Income Tax - “Salary”

HRA Exemption

- Rent paid receipt is an crucial document evidencing your claim of allowance which should include complete details of rental payments, name of landlord, PAN, period, etc. and duly signed / stamped by the landlord.
- Providing a copy of rental agreement or lease deed can further substantiate your claim of allowance. It serves as a legal proof of your tenancy and strengthen your HRA claim

Income Tax - “Salary”

HRA Exemption

HRA Calculation

Special allowance to meet expenditure on payment of rent, least of the following:

In Mumbai / Delhi / Kolkata / Chennai	In Other Cities
1) HRA Allowance actually received	1) HRA Allowance actually received
2) Rent paid in excess of 10% of Salary	2) Rent paid in excess of 10% of Salary
3) 50% of Salary	3) 40% of Salary

Salary includes DA, however it excludes other allowances and perquisites

Case Law

Aman Kumar Jain vs. ITO, ITA No. 267/Del/2023 (ITAT) Delhi

- Husband was paying rent to his wife who owned the residential property and claimed HRA deduction u/s 10(13A) of the Act.
- The said residential property was purchased by wife by procuring loans from bank and she also paid interest and instalments.
- Wife offered the said rental payments received from husband as “Income from House Property” in her return of income.
- Apart from rental income, wife also had independent income which was offered for tax under the head “Business Income” and “Income from other Sources”
- CIT(A) had disallowed the deduction – no other income apart from rent & earning nominal income.
- Based on the facts of the case and legitimacy of deduction, assessee’s appeal was allowed by Hon’ble ITAT Delhi.

Case Law

Abhay Kumar Mittal vs. DCIT 3385 Delhi 2019 (ITAT Delhi)

- The issue before the bench was whether the rent paid to wife is allowed as a deduction from House Rent Allowance (HRA) and is subject to clubbing provisions in the hands of husband.
- The Income Tax Act does not prohibit claiming HRA exemption on the rent paid to one's spouse. The wife was a qualified professional and was filing her return of income regularly.
- The wife obtained loan from husband for acquiring property, which she later on repaid from investment proceeds.
- The rent receipts were offered for tax under the head "Income from house property" of the wife.
- Based on the facts of the case, documents produced, Income being offered for tax, etc. Tribunal allowed the appeal.

key takeaways

- The Income Tax Act does not debar claiming HRA exemption on rent being paid to one's spouse.
- In the eyes of the law, both husband and wife are different persons. The contention that the transaction between husband and wife are not commercial and a meagre arrangement does not hold merit.
- Fact that the scale / level of income can decide the fate whether a capital asset can be purchased by the assessee, needs a look depending on case to case.
Sources of funds needs to be identified, Capital Income, etc.
- HRA granted to an employee who is residing in a house owned by him does not qualify for exemption.

Income Tax - “Salary”

Disclosures

Disclosure of Salary components in Return of Income

PART B GROSS TOTAL INCOME				Whole- Rupee(₹) only
B1	i	Gross Salary (ia + ib + ic+id+ie)	i	
		a Salary as per section 17(1)	ia	
		b Value of perquisites as per section 17(2)	ib	
		c Profit in lieu of salary as per section 17(3)	ic	
		d Income from retirement benefit account maintained in a notified country u/s 89A (country drop down will be provided in e-filing utility)	id	
		e Income from retirement benefit account maintained in a country other than notified country u/s 89A	ie	
	ii	Less allowances to the extent exempt u/s 10 (drop down to be provided in e-filing utility) (Ensure that it is included in salary income u/s 17(1)/17(2)/17(3))	ii	
	iiia	Less: Income claimed for relief from taxation u/s 89A	iiia	
	iii	Net Salary (i – ii-iiia)	iii	
	iv	Deductions u/s 16 (iva + ivb + ivc)	iv	
		a Standard deduction u/s 16(ia)	iva	
		b Entertainment allowance u/s 16(ii)	ivb	
		c Professional tax u/s 16(iii)	ivc	
	v	Income chargeable under the head ‘Salaries’ (iii – iv)	B1	

SALARY / PENSION

Income Tax - “Salary”

Disclosures

Disclosure of Directorship in Return of Income:

Whether the assessee is Director in a Company?

	(i)	Whether you were Director in a company at any time during the previous year? (Tick) <input checked="" type="checkbox"/> Yes <input type="checkbox"/> No				
		If yes, please furnish following information -				
		Name of Company	Type of company	PAN	Whether its shares are listed or unlisted	Director Identification Number (DIN)

Income Tax - “Salary”

Disclosures

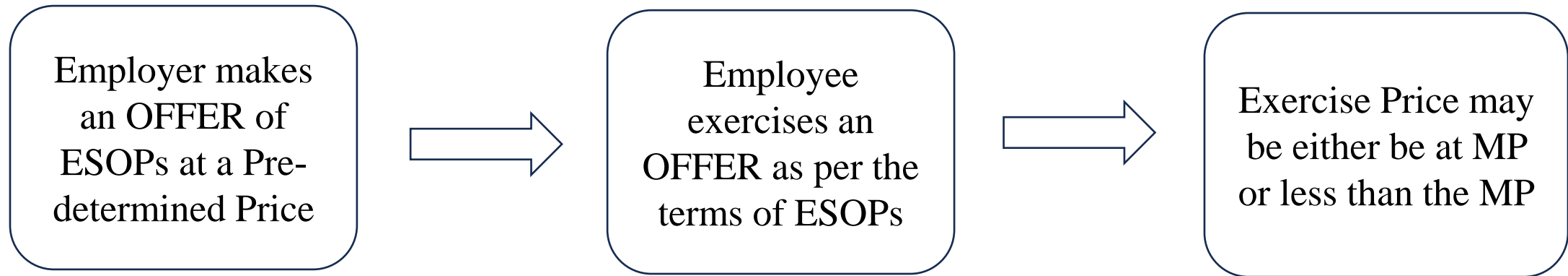
Disclosure of TDS on Salary in Return of Income:

Do ensure to disclose details of Gross Salary as per Form 16 – Details of Tax Deducted at Source [As per form 16 issued by employer]

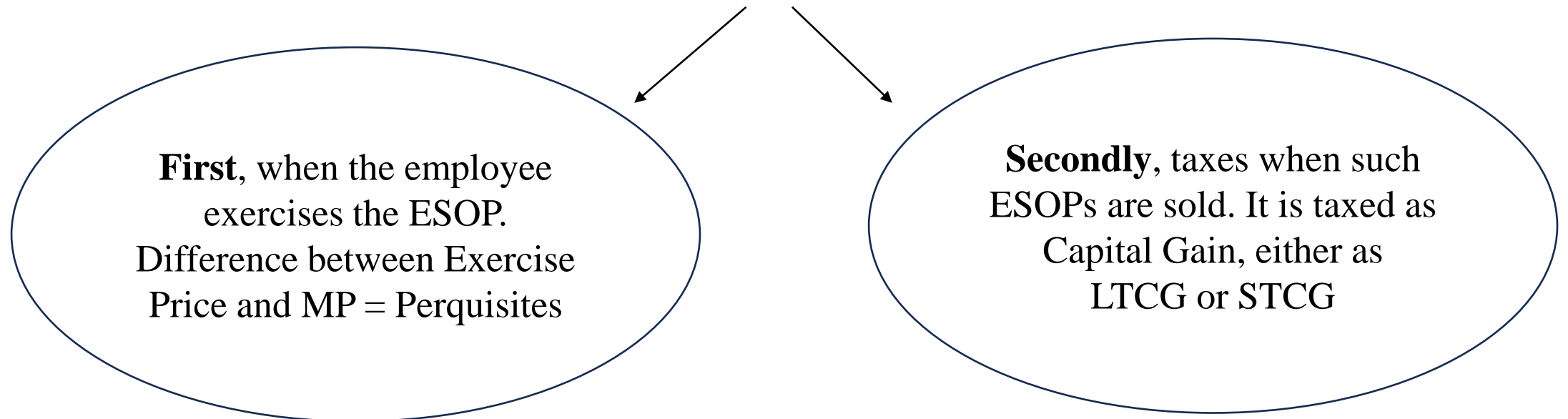
B		Details of Tax Deducted at Source from Salary [As per Form 16 issued by Employer(s)]				
TDS ON SALARY	Sl No	Tax Deduction Account Number (TAN) of the Employer	Name of the Employer	Income chargeable under Salaries	Total tax deducted	
	(1)	(2)	(3)	(4)	(5)	
	I					

Income chargeable under Salaries (column 4) should match with Income chargeable under the head Salary in Schedule S

ESOP's broad framework



Taxation of ESOP's



ESOP's

- Employee Stock Option Plan (ESOP) is a popular long term incentive initiated by the employers (companies) which is basically to attract, retain and provide reward employees.
- It also provides employees to be a part of the company, whereby they are provided an opportunity to become a shareholder and be a part of company's growth.
- ESOP's and its variants are one of the popular framework for "Start-Ups"
- It is usually granted to eligible employees, who may exercise the option at a pre-determined price.

ESOPs taxation

Taxation of ESOPs:

- Considering the proposal of ESOP (i.e. grant, vesting period, exercise), it is at most important to know the taxability provisions under Income Tax Act 1961. As per the Income Tax Act 1961, the tax implications gets triggered at two stages:

1) At the time of exercise of the Option – under “Salary”

2) At the time of sale of shares (ESOP) – under “Capital Gains”

1) At the time of Exercise of the Option

- It is the first taxable event in the hands of the employees and taxed as a perquisite under the head “Salary”
- Value of Perquisite = Difference between the Fair Market Value (FMV) on date of exercise as reduced by the exercise price (actual price) x Shares Allotted
- On the said perquisite the employer is required to deduct tax at source and the same gets reflected in Form 16 – Annexure Form 12BA.

ESOPs taxation

As per Income Tax rules, FMV for this purpose would be as under:

- **Listed Shares**

Fair Market Value (FMV) shall be the average of the opening price and closing price of the share on stock exchange on the date of exercise of the options.

- **Unlisted Shares**

Fair Market Value (FMV) of shares shall be determined by a Merchant Banker on the specified date

ESOPs taxation

- **Deferment of withholding tax (Budget 2020 – Amendment)**

Employees receiving ESOPs from eligible startups do not have to pay tax in the year of exercise of option, but is to be paid (whichever is earlier):

- Expiry of 5 years from year of ESOP allocation
- Date of sale by the employee
- Date of termination of employment

Eligible Startups refers to startup that are registered with Government and holds a certificate of eligible business from Inter-Ministerial Board (IMB) Certification.

ESOPs taxation

2) At the time of Sale of Shares (ESOP)

- At the time of sale of share it is taxed under the head “Capital Gains” and capital gain tax is attracted.
- Capital Gain will be computed on the difference between Sale Price and the FMV of the shares as on date of exercise of the option (which was considered and taxed as perquisite)
- Capital Gains is further classified as “Short Term Capital Gain” or “Long Term Capital Gain” based on period of holding. The period of holding is considered from the date of allotment of shares.
- Unlisted shares should be held for more than 24 months to qualify as Long Term Asset
- Listed shares should be held for more than 12 months to qualify as Long Term Asset

ESOPs taxation

Listed on Recognised Stock Exchange

- Long Term Capital Gains – Gains exceeding Rs. 100,000/- are taxed @10% without indexation benefit
- Short Term Capital Gains – Taxable @15%

Not listed on Recognised Stock Exchange

- Long Term Capital Gains – Taxable @20% (with indexation benefit)
- Short Term Capital Gains – Sales Consideration as reduced by the Cost of acquisition is taxed as per the slab rates of the individual

ESOP of an Foreign Company

- Tax treatment is not very different from the tax treatment of ESOPs of Indian entities.
- It is possible that ESOP of foreign company is taxed in the country in which it is listed or the company is headquartered. In such a case DTAA benefit can be sought.

ESOP disclosure requirements

Reporting requirements in tax return:

- Details of shares held in unlisted company, needs to be reported by the employee in return of income.
- Shares of foreign entity allotted under an ESOP to employee of its group entity would also be considered as shares of an unlisted company. However in such a case additional requirement needs to be done.
- Shares allotted by Foreign Company to an employee (resident), it qualifies as “Foreign Asset” and requires disclosure under **Schedule FA** of income tax return.
- If the employees total income exceeds Rs. 50 lakhs, then **Schedule AL** needs to be reported wherein cost of acquisition of foreign asset needs to be disclosed.

Recent Developments

Is AIS fully reliable for ITR filings?

- Merely relying on Annual Information System (AIS) to file return of income may invite trouble going ahead. This is because there are certain transactions which are not reflected in AIS and if the Income Tax authorities comes to know about this then it can send you notice – 133(6)
- Interest Income from RBI floating rate bonds (taxable), PPF (not taxable)
- Incorrect reporting of Interest Income on Savings account, Fixed Deposit Interest, etc.
- It is always a healthy practice to report exempt income in return of income
- Details of **rental income earned (by landlord)** will also be disclosed in AIS – the same is reported by **employer of a person claiming HRA exemption.**
- Make sure that **return of income filed is E-verified** within 30 days of filing.

Recent Development

THE ECONOMIC TIMES | News
English Edition ▾ | Today's Paper

Subscribe | Sign in
Special Offer on ET Prime

Home ▶ ETPrime Markets **News** Industry Rise Politics Wealth Mutual Funds Tech Careers Opinion NRI Panache ET NOW Spotlight ⋮

India Decoded Web Stories Morning Brief Podcast Newsblogs **Economy** ▾ Industry Politics Company ▾ Defence ▾ More ▾

Business News › News › Economy › Policy › Salaried individuals under I-T scanner as taxman serves notices asking assesseees for documentary proof to claim exemption

ETPrime

Salaried individuals under I-T scanner as taxman serves notices asking assesseees for documentary proof to claim exemption

If disclosure requirements are correctly made and legitimate tax deductions / exemption are availed, then there is no need to be concerned.

Form 16

FORM NO. 16

[See Rule 31(1)(a)]

PART A

Certificate under section 203 of the Income-tax Act, 1961 for Tax deducted at source on Salary paid to an employee under section 192 or pension/interest income of specified senior citizen under section 194P

Certificate No.		Last updated on	
Name and address of the Employer /Specified Bank		Name and address of the Employee /Specified senior citizen	
PAN of Deductor	Tan of the Deductor	PAN of the Employee/Specified senior citizen	Employee Reference No./ Pension Payment order no. provided by the Employer(If available)
CIT(TDS)		Assessment year	Period with the Employer
Address :		From	To
City :	Pin code :		

Form 16

Summary of amount paid/credited and tax deducted at source thereon in respect of the employee

Quarter(s)	Receipt Numbers of original quarterly statements of TDS under sub-section (3) of section 200	Amount paid/credited	Amount of tax deducted (Rs.)	Amount of tax deposited/remitted(Rs.)
Quarter 1				
Quarter 2				
Quarter 3				
Quarter 4				

Total (Rs.)

Form 16

II.DETAILS OF TAX DEDUCTED AND DEPOSITED IN THE CENTRAL GOVERNMENT ACCOUNT THROUGH CHALLAN

(The deductor to provide payment wise details of tax deducted and deposited with respect to the deductee)

Sl.No	Challan Identification Number (CIN)				
	Tax Deposited in respect of the deductee (Rs.)	BSR Code of the Bank Branch	Date on which tax deposited (dd/mm/yyyy)	Challan Serial Number	Status of matching with OLTAS
Total(Rs.)					

Verification

I _____, son/daughter of _____ working in the capacity of _____ (designation) do hereby certify that a sum of Rs. _____ [Rs. _____ (in words)] has been deducted and deposited to the credit of the Central Government. I further certify that the information given above is true, complete and correct and is based on the books of account, documents, TDS statements, TDS deposited and other available records.

Place

Date

(Signature of person responsible for deduction of tax)

Full Name :

Please ensure that correct details are disclosed in Form 26AS of Employee which also corresponds to Form 16.



THANK
YOU

CA Chintan Vasani
vasani.chintan@shahgupta.com