

## Tax management Answers for IAT 2

### Part a

1.

#### Definition of Word 'Salary' [Sec. 17(1)]

**According to Section 17(1) salary includes the following amounts received by an employee from his employer, during the previous year**

- 1. Wages;**
- 2. any annuity or pension; (Family pension received by heirs of an employee is taxable under income from other sources);**
- 3. any gratuity;**
- 4. any fees, commission, perquisites or profits in lieu of or in addition to any salary or wages;**
- 5. any advance of salary;**
- 6. any payment received by an employee in respect of any period of leave not availed of by him; (Leave encashment or salary in lieu of leave);**
- 7. the annual accretion to the balance at the credit of an employee participating in a recognised provident fund, to the extent to which it is chargeable to tax under Rule 6 of part A of the Fourth Schedule; and**
- 8. the aggregate of all sums that are comprised in the transferred balance as referred to in sub-rule (2) of Rule 1] of Part A of the Fourth Schedule, of an employee participating in a recognised provident fund, to the extent to which it is chargeable to tax, under sub-rule (4) there, i.e.,**

*taxable portion of transferred balance from unrecognised provident fund to recognised provident fund.*

9. the contribution made by the Central Government or any other employer in the previous year, to the account of an employee under a pension scheme referred to in Section 80CCD.

## B. Types of Provident Funds : Tax Implications & Key Points

- **Statutory Provident Fund (SPF / GPF)**
  - These are maintained by Government, Semi Govt bodies, Railways, Universities, Local Authorities etc.,
  - The contributions made by the employer are exempted from income taxes in the year in which contributions are made.
  - The contributions made by the employee can be claimed as tax deductions **under section 80c**.
  - Interest amount credited during the financial year is not treated as income and hence it is exempted from income tax.
  - The redemption amount at the time of retirement is exempted from tax.
  - If an employee terminates the PF account, the withdrawal amount too is exempted from taxes.
- **Recognized Provident Fund (RPF)**
  - Any establishment (business entity) which **employs 20 or more** employees can join RPF. Most of the individuals (*who are salaried*) generally contribute to this type of Provident Fund. This is one of the

popular types of [Employees Provident Funds](#) (EPF). (*Organizations which employ less than 20 employees can also join RPF if the employer and employees want to do so*)

- The business entity can either join the Govt. scheme set up by the PF Commissioner (or) the employer himself can manage the scheme by creating a PF Trust. All Recognized Provident Fund Schemes must be approved by The Commissioner of Income Tax (CIT).
- Employer's contribution **in excess of 12% of salary** is treated as income of the employee and is taxable. In excess of 12%, the contributions are taxable in the year of contribution.
- Tax Deduction **u/s. 80C** is available for amount invested by the employee (*up to Rs 1.5 Lakh in a Financial Year*).
- Interest amount earned (up to 9.5% interest rate) on PF balance (employee's + employer's contributions) is tax free. **In excess of 9.5%**, the interest on contributions is taxable as 'salary' in the year in which it is accrued.
- Accumulated funds redeemed by the employee at the time of retirement / resignation are exempt from tax if he/she continues the service for **5 years** or more.
- **Unrecognized Provident Fund (UPF)**
  - These are not recognized by Commissioner of Income Tax.
  - Employer's contribution is not treated as income in the year of investment and hence not taxable in that specific year. So, it is tax free in the year of contribution.
  - Tax deduction under **section 80c is not available** on Employees contributions.

- Interest earned is not treated as income in the year it is credited and hence not taxable in the year of accrual.
- At the time of redemption / retirement, the employer's contributions and interest thereon is treated as 'salary income' and chargeable to tax. However, employee's contribution is not chargeable to tax. Interest on Employees contribution will be charged under income from other sources.
- **Public Provident Fund (PPF)**
  - Under PPF any individual from public, whether is in employment or not may contribute to this fund.
  - The minimum contribution is Rs. 500 p.a. & maximum is Rs 1.5 Lakh Rs. p.a. The amount is repayable after 15 years.
  - PPF can serve as an excellent retirement planning / savings tool, for those who do not come under any pension scheme.
  - The PPF offers tax benefit under **section 80C** and the interest earned is also exempt from tax. All the eligible withdrawals are exempted from taxes.

C.

Computation of salary income of Mr.N for the A.Y 2018-19.

Basic salary	96,000
Dearness allowance	24,000
Bonus	8,000
Commission	4,500

Entertainment Allowance		6,000
Rent free accommodation	18,615	
Value of furniture	2,000	20,615

Total salary income of Mr N for the A.Y 2018-19 is Rs. 1,59,115.

## 2.a Gross annual Value

In the case of self-occupied property, the annual value is taken to be 'nil'. In the case of property that is rented out, the gross annual value is the municipal value, the de facto rent (whether received or receivable) or the fair rental value, whichever is highest. If, however, the Rent Control Act applies to the property, the gross value cannot exceed the de facto rent or the standard rent under the Rent Control Act, whichever is higher.

b. Perquisites exempt from tax are:

Provision of medical facilities (Provision to Sec. 17(2)): Value of medical treatment in any hospital maintained by the Government or any local authority or approved by the Chief Commissioner of Income-tax. Besides, any sum paid by the employer towards medical reimbursement other than as discussed above is exempt upto Rs.15,000/-.

Perquisites allowed outside India by the Government to a citizen of India for rendering services outside India (Sec. 10(7)). Rent free official residence provided to a Judge of High Court or Supreme Court or an Official of Parliament, Union Minister or Leader of Opposition in Parliament.

No perquisite shall arise if interest free/concessional loans are made available for medical treatment of specified diseases in Rule 3A or where the loan is petty not exceeding in the aggregate Rs.20,000/-No perquisite shall arise in relation to expenses on telephones including a mobile phone incurred on behalf of the employee by the employer.

### c.Income from salary of Miss R for the A.Y 2018-19

Basic salary	1,92,000
D.A	12,000
HRA	Nil
Conveyance allowance 800-600	2,400
CCA 150 x12	1800
Motor car 2400 + 900 x 12	39,600
LIC	8,000
Children education allowance 7200-2400	4,800
Contribution to RPF 14%-12%= 27720-23760	3,960
Interest on RPF 12.5%-9.5% = 6875-5225	1650
<b>Total</b>	<b>2,66,210</b>

### 3.a Depreciation

1. A noncash expense that reduces the value of an asset as a result of wear and tear, age, or obsolescence. Most assets lose their value over time (in other words, they depreciate), and must be replaced once the end of their useful life is reached. There are several accounting methods that are used in order to write off an asset's depreciation cost over the period of its useful life. Because it is a non-cash expense, depreciation lowers the company's reported earnings while increasing free cash flow.

b. Taxable income of Mr X from business for the A.Y 2018-19.

Net profit		88,000
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Add: Inadmissible expenses

Salary	12,000	
Legal expenses	2,000	
Expenses on patent	14,000	
Donation	4000	
Provision for B.debts	6,000	38,000

Less:

Bad debts received	12,000	
Dividend	6,000	
Rent from HP	18,000	
Share of income from HUF	6,000	42,000

Taxable income from business is Rs.84,000.

#### Part B

4.a

Fair market value of the House property	72,000
Less: Municipal taxes	7,200

Net annual value is	64,800
Less 30 % standard deduction	19,440

Income from HP for the A.Y is Rs. 45,360.





Fund	During Service / Contribution Period			Retir
	Employee's Contribution	Employer's Contribution	Interest on PF	
SPF	Deduction u/s 80c is available	Tax-free	Fully exempt	
RPF	Deduction u/s 80c is available	Exempt upto 12% of Salary	Exempt upto 9.5%	* Em * Wl years (o * PF
UPF	Tax Deductions not available	Not taxable	Not taxable	Emp the Emp t cont
PPF	Deduction u/s 80c is available	Not Applicable	Fully exempt	

