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CIRCULAR

Sub: Changes made by the Finance Act, 2020, affecting taxation of employees

The Finance Act, 2020, has made a certain changes in the provisions of Income-tax Act, 1961 (Act), which affect the taxability of employees (including ex-employees) for and from the Financial Year (FY) 2020-21 in respect of their income from salaries and the deductions usually admissible to them. These changes are summarized hereinbelow.

1. Amendments in provisions relating to Residential Status

(i) Reduced period of stay in India for determining residential status in certain cases

Section 6 of the Act brings out parameters to determine residential status of a person. As per the pre-amended provisions of sub-section (1) of section 6 of the Act, an individual is considered as resident in India for a financial year if-

(a) he is in India for 182 days or more during that financial year; or

(b) he has been in India for 365 days or more during the four immediately preceding financial years and for 60 days or more during the relevant financial year.

Explanation 1(a) to the aforesaid section 6(1) provides that, in respect of an Indian citizen who leaves India in any financial year for the purpose of employment outside India, the period of 60 days as mentioned in (b) above shall be substituted with 182 days. Explanation 1(b) to section 6(1) provided similar concession in respect of an Indian citizen and a person of Indian origin who visits India during the relevant financial year.

The Finance Act, 2020, has amended Explanation 1(b) to section 6(1) of the Act to reduce the period of stay brought out therein from 182 days to 120 days in the case of the citizen or person of Indian origin having total income, other than the income from foreign sources, exceeding ₹ 15 lakh during the relevant financial year.

Accordingly, an Indian citizen or a person of Indian origin who visits India in any financial year and whose total income for that financial year (excluding income from foreign sources) exceeds ₹ 15 lakh would be considered as resident in India if-

(a) he stays in India for 182 days or more during that financial year; or

(b) he has been in India for 365 days or more during the four immediately preceding financial years and for 120 days or more during the relevant financial year.

(ii) <u>Provision of "Deemed Residence"</u>

A new sub-section (1A) has been inserted under section 6 of the Act which provides that, an individual being a citizen of India would be deemed to be a resident in India for a financial year if-

(a) total income of the individual (other than income from foreign sources) for the relevant financial year exceeds ₹ 15 lakh; and

(b) the individual is not liable to pay tax in any other country or territory by reason of his domicile or residence or any other criteria of similar nature.

If an individual is covered within the ambit of the aforesaid section 6(1A) of the Act for a financial year, he will be considered as a resident in India irrespective of his period of stay in India during the financial year.

(iii) <u>Residents under the amended provisions to be considered as "Not Ordinarily Residents"</u>

The provisions of sub-section (6) of section 6 have also been amended to provide that the following persons would be considered as resident but not ordinarily resident in India during a financial year-

(a) a citizen of India, or a person of Indian origin, having total income, other than the income from foreign sources, exceeding ₹ 15 lakh during the relevant financial year, as referred to in Explanation 1(b) to section 6(1) of the Act, who has been in India for a period of 120 days or more but less than 182 days.

In other words, a person who is considered a resident in India by virtue of stay in India for the reduced period of 120 days as per the amended provisions of Explanation 1(b) to section 6(1) of the Act; and

(b) an Indian citizen who is deemed to be an Indian resident under newly inserted sub-section (1A) of section 6 of the Act.

Consequently, income of such residents which accrues or arises to them outside India shall not be included in their total income unless it is derived from a business controlled in or a profession set up in India.

Further, for the purposes of (i) (ii) and (iii) above, "income from foreign sources" also means income which accrues or arises outside India (except income derived from a business controlled in or a profession set up in India).

2. <u>New Concessional Tax Regime for Individuals</u>

While there has been no change in rates of tax applicable to different slabs of income in case of individuals, *a new section 115BAC has been inserted which provides an*

option to the individuals to be taxed at the lower income-tax rates as brought out therein subject to satisfaction of certain conditions as specified therein.

The option to avail the new regime has to be exercised by the employee at the time of filing its Return of Income for an assessment year.

(i) Rates of tax under the new regime

Under the aforesaid regime, the tax rates applicable to the different slabs of income of an individual are as under-

Income (₹)	***Tax Rate***
Upto 2,50,000	*Nil*
2,50,001 to 5,00,000	*5%*
5,00,001 to 7,50,000	*10%*
7,50,001 to 10,00,000	*15%*
10,00,001 to 12,50,000	*20%*
12,50,001 to 15,00,000	*25%*
Above 15,00,000	*30%*

(ii) Non-availability of exemption u/s. 10 of the Act

*If an employee opts for the aforesaid new regime, following exemptions **would not be available** to the employee-*

(a) Exemption u/s. 10(5) of the Act in respect of leave travel assistance received from the employer;

(b) Exemption u/s. 10(13A) of the Act in respect of House Rent Allowance;

(c) Exemption u/s. 10(14) of the Act in respect of certain prescribed allowances granted by an employer to meet (i) expenses incurred exclusively for official purposes; or (ii) personal expenses of the employee;

However, section 115BAC provides that exemption u/s. 10(14) would continue to be available in respect of certain allowances to be prescribed by the Central Board of Direct Taxes (CBDT). No allowance has so far been prescribed by the CBDT in this regard.

(d) Exemption u/s 10(32) in respect of clubbing of income of a minor child.

(iii) Non-availability of certain deductions against the income

*The employee availing the new regime **would not be entitled** to the following deductions available under the existing regime-*

(a) Standard Deduction upto ₹ 50,000 available under section 16 of the Act against salary income;

(b) Deduction in respect of interest on loan taken for a self-occupied house property upto ₹2 lakh under section 24(b) of the Act;

(c) Deduction of 33.33% of income or ₹ 15,000, whichever is less, under section 57(iia) of the Act in respect of family pension;

(d) Deductions under Chapter VI-A (section 80C to section 80U). However, deduction u/s. 80CCD in respect of employer's contribution to NPS would continue to be available.

The employee would also not be entitled for set off of any loss under the head "income from house property" against income of any other head. The exemption, deduction, if any, available in respect of allowance or perquisite under any other law would also not be available under the new regime.

Note- The requirement of TDS from salary payments is determined by taxability thereof in the hands of the employee. Thus, if an employee is willing to opt for the new regime, the salary income should be calculated by the employer under the provisions of new regime and TDS should be regulated accordingly.

However, on a literal interpretation of the provisions of the Finance Act, 2020, it appears that, while an employee has the option to avail the aforesaid new regime or continue to be taxed under the existing regime, no such option is available to the employer for TDS purposes and TDS has to be regulated as per the existing regime only. Till the time the issue is clarified by CBDT, TDS on income of all employees (including the employees who are willing to opt for the new regime) would continue to be calculated as per existing regime only.

3. Overall ceiling for Employer's Contribution to CPF, approved Superannuation Fund and NPS

The contribution by the employer to the account of an employee in a recognized provident fund exceeding 12% of salary is taxable as salary in the hands of the employee. Further, under the provisions of section 17(2) of the Act, the amount of any contribution to an approved superannuation fund by the employer exceeding ₹ 1.5 lakh is treated as perquisite in the hands of the employee. Similarly, an assessee is allowed deduction under National Pension Scheme (NPS) @ 14% of the salary contributed by the Central Government and @ 10% of the salary contributed by any other employer.

The provisions of section 17(2) have been amended to provide an overall ceiling of ₹ 7.5 lakh in respect of employer's contribution to the aforesaid funds/scheme. As per the amended provisions, any contribution made to the account of an employee by the employer-

(a) in a recognised provident fund;

(b) in a scheme referred to in section 80CCD(1) of the Act i.e., NPS; and

(c) in an approved superannuation fund

in excess of ₹ 7.5 lakh during a financial year would result in perquisite in the hands of the employee and would be taxable as salary income.

Thus, while employer's contribution to a recognised provident fund in excess of 12% of salary of the employee would continue to be taxed as salary income of the employee and deduction in respect of employer's contribution to NPS would continue to be available only upto 10% of salary income of the employee, if aggregate of the contributions made by the employer to a recognised provident fund, NPS and approved superannuation fund (PRBS) exceeds ₹ 7.5 lakh during a financial year, such excess would be taxable as salary income of the employee.

A new clause (viia) has also been inserted under section 17(2) of the Act to provide that the annual accretion by way of interest, dividend or any other amount of similar nature during a financial year to the balance at the credit of recognised provident fund, NPS and approved superannuation fund to the extent the same relates to the contribution which is included in the total income of the employee (i.e., contribution in excess of ₹ 7.5 lakh) would also result in perquisite in the hands of the employees and would be taxable as salary income of the employee.

It has, however, been provided under the above clause that, the taxable income in respect of interest, dividend etc., would have to be computed in the manner as may be prescribed by CBDT. No computational methodology has, so far, been prescribed by CBDT in this regard.

3. Extending time limit for sanctioning of loan for affordable housing for availing deduction under section 80EEA of the Act

The provisions of section 80EEA of the Act provide for a deduction in respect of interest on loan taken from any financial institution for acquisition of an affordable residential house property. The deduction is allowed up to ₹ *1.5 lakh* and is subject to certain conditions as specified therein. As per the pre-amended provisions, one of the conditions is that loan sanctioned by the financial institution should have been during the period from 1st April, 2019 to 31st March, 2020.

The provisions of section 80EEA have been amended to extend the period of sanctioning of loan by the financial institution from 31st March, 2020 to 31st March, 2021.

This circular has been compiled by Corporate Tax Division for basic guidance of the concerned persons. Only highlights of significant amendments have been brought out hereinabove and this circular does not purport to be an exhaustive document covering all facets of deduction of tax at source from salaries. The concerned persons are, therefore, requested to consult the relevant Acts, Rules, Notifications, Circulars, etc., including the detailed circular issued by Central Board of Direct Taxes every year in regard to TDS from salaries, and to exercise all due care and caution while effecting deduction and deposit of tax at source.

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