Taxability of living allowance due to lockdown

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Lockdown has led to employees stranded at a place other than their place of residence/ employment, either in India or outside India.

To help these employees, their respective employers have either paid them living allowance (to meet their expenses on food, rent, electricity, laundry, etc.) or have provided them rent-free accommodation/ hotel accommodation at such a place.

In this article, we have discussed the tax implication of living allowance paid to the employees and the rent-free accommodation/ hotel accommodation provided to the employees due to lockdown.

Taxation of living allowance:

As per Section 10(14)(i) of the Income-tax Act, 1961 (Act) read with Rule 2BB of the Income-tax Rules, 1962 (Rules), living allowance paid to the employees, specifically to meet the expenses wholly, necessarily and exclusively incurred, in the performance of official duties, while such employees are on tour or transfer, is exempt from tax in the hands of such employees to the extent such allowance is actually incurred for the said purpose.

When the employees are stranded at a place other than their regular place of employment, one will have to evaluate whether the employees are on 'tour' or on 'transfer' for the performance of official duties, or not and if not, living allowance paid to such employees will be liable to tax as salary.

Please note that one will have to examine the facts and circumstances of the case (specifically the employment contract, employment structure, terms and conditions of employment, the period of work, etc.) in detail to evaluate this aspect.

To do so, one can refer to the decision of the Kolkata Bench of Income Tax Appellate Tribunal (ITAT) in the case of ITO v Saptarshi Ghosh [2011] 15 taxmann.com 328 (Kolkata) wherein the ITAT has nicely explained the difference between 'tour' and 'transfer.' Nonetheless, let's understand this aspect by way of simple examples:

Example 1: An employee having a place of employment in Mumbai had gone to Mauritius on vacation with his family and is now stranded in Mauritius due to lockdown. His employer has paid him living allowance to meet his expenses. In such situation, one cannot say that the employee was on 'tour' or on 'transfer' for official purposes and hence living allowance paid to such employee should be charged to tax as salary.

Example 2: An employee having a place of employment in Mumbai had gone to Mauritius to work on a project of one of the clients of his employer. Such employee is now stranded in Mauritius due to lockdown. His employer has paid him living allowance to meet his expenses. In such situation, it can be said that an employee was on tour for official purposes and hence living allowance paid to such employee should be exempt from tax as per Section 10(14)(i) of the Act read with Rule 2BB of the Rules to the extent such living allowance is actually incurred in performance of official duties.

To avoid any adverse tax consequences, it is advisable that the employees maintain a copy of the bills/ invoices evidencing the nature of expenses, amount of expenses, date and place where the expenses are incurred etc., in the absence of which, tax authorities are likely to tax the amount of living allowance paid in the hands of the employees as salary.

Taxation of rent-free accommodation/ hotel accommodation:

As per Section 17(2) of the Act, rent-free accommodation/ hotel accommodation provided by the employer to its employee is a perquisite and hence value of such rent-free accommodation/ hotel accommodation is charged to tax as salary.

But, due to lockdown, when the employees are stranded at a place other than their regular place of employment and if such employees are provided with rent-free accommodation/ hotel accommodation so that such employees can perform official duties, then can one say that such rent-free accommodation/ hotel accommodation is a perquisite as per Section 17(2) of the Act and accordingly, value of such rent-free accommodation/ hotel accommodation should be charged to tax as salary?

To help such employees, take appropriate positions in their return of income, we have discussed below few interesting decisions on the issue – please note that there are many decisions on this issue – for the purpose of this article, we have restricted our discussion to only three decisions.

(*a*) Decision of the Calcutta High Court (HC) in the case of CIT v D. S. Blackwood [1989] 46 Taxman 322 (Cal):

The assessee was a permanent employee of John Brown Engineering (Clyde Bank) Ltd. (JBE), Scotland, U.K. JBE had entered into an agreement with the West Bengal State Electricity Board for erection of gas turbines at Kasba (Calcutta), Siliguri and Haldia, pursuant to which, the assessee-engineer was deputed to India, from time to time to supervise the erection work. While staying in India, the assessee was provided with rent-fee accommodation. The Income Tax Officer (ITO) was of the view that rent-free accommodation provided by JBE was in the nature of perquisite and hence, added a sum of Rs. 40,111 as perquisite as per Rule 3 of the Rules. The assessee preferred an appeal before the Commissioner of Income-tax (Appeals) [CIT(A)], who deleted the addition of Rs. 40,111 on the ground that the assessee was on tour to India and the benefit of rent-free accommodation was exempt under Section 10(14) of the Act. Now, revenue preferred an appeal before the Calcutta Bench of ITAT and there was a difference of opinion and ultimately by a majority decision, the Calcutta Bench of ITAT upheld the view taken by the CIT(A). On these facts, the Calcutta Bench of ITAT then referred the following question under Section 256(1) of the Act to the Calcutta HC for the Assessment Year (AY) 1979-80:

"Whether, on the facts and in the circumstances of the case, the Tribunal was justified in law in holding that the rent-free accommodation provided to the assessee by his employer was exempt under Section 10(14) of the Act?"

The Calcutta HC answered the aforesaid question as under:

"Section 10(14) provides that in computing the total income of a person, any special allowance or benefit, not being in the nature of entertainment allowance or other perquisite within the meaning of clause (2) of section 17, specifically granted to meet expenses wholly, necessarily and exclusively incurred in the performance of the duties of an office or employment of profit, to the extent to which such expenses are actually incurred for that purpose, shall not be included.

Here, the assessee was provided with rent-free accommodation by his employer while he was on tour in India. It has been found by the Tribunal as a fact that the rent-free accommodation was provided by the foreign company to the assessee necessarily for the discharge of his official duty for which he was sent to India. He visited India several times between May 1977 and March 1980. ***The assessee was not occupying the rent-free accommodation by virtue of his posting as an employee of the foreign company in Calcutta.*** *It is in connection with his official duty for the purpose of supervising the erection of gas turbines at Calcutta, Siliguri and Haldia that the assessee had to visit these places. Such visits are in*

connection with his official duty. In the premises, the expenditure which has been incurred must be held to be wholly and exclusively incurred for the purpose of performing his official duties. This expenditure, on these facts, cannot be treated as a benefit given to the assessee."

In a nutshell, the Calcutta HC said that the rent-free accommodation provided to the employees while on tour in performance of official duties is not a benefit given to the employees and hence, value of such rent-free accommodation is exempt from tax as per Section 10(14) of the Act.

(*b*) Decision of the Delhi Bench of ITAT in the case of Hyundai Heavy Ind. Co. Ltd. v ITO [1994] 51 ITD 34 (Delhi):

In this case, the assesses were the employees of Hyundai Heavy Ind. Co. Ltd. (HHI), a company incorporated in Korea and were rendering services in India pursuant to a contract between HHI and ONGC. These assessees were provided with free boarding and lodging facilities while they were working on different installations. HHI filed the return of income of these assessees as a representative assessee, declaring NIL income, after claiming salary paid for the period during which services were rendered in India as exempt from tax in India, as per the DTAA between India and Korea. ITO taxed the amount of salary so paid. The assesses preferred an appeal before the CIT(A) who upheld the order of the ITO. The assesses preferred a further appeal before the Delhi Bench of ITAT.

In the meantime, the Commissioner of Income-tax passed an order under Section 263 of the Act revising the order of ITO after assessing the value of free boarding and lodging facilities as perquisite as per Section 17(2) of the Act. The assesses preferred an appeal before the Delhi Bench of ITAT against the said order under Section 263 of the Act.

At the outset, the Delhi Bench of ITAT referred the dictionary meaning of the expression 'perquisite' and many other decisions to understand the meaning of this expression 'perquisite'. An interesting decision which was referred was that of the Gujarat HC in the case of CIT v S. G. Pgnatale [1980] 124 ITR 391 (Guj) wherein the Gujarat HC had said that 'perquisite' is something which arises by reason of personal advantage and would not apply to mere reimbursement of necessary disbursement and that this principle was well recognised in House of Lords' decision in Owen v Poor (Inspector of Taxes) [1969] 74 ITR 147 (HL). Further, the Gujarat HC had said that the expression 'perquisite' in Section 17(2) of the Act has been defined in an inclusive manner and hence the ordinary meaning of the expression would prevail. The Delhi Bench of ITAT then also referred the decision of the Calcutta HC (Supra) and acknowledged the principle laid down therein saying:

"No doubt, the aforesaid decision pertains to the provisions of section 10(14), but applies to the facts of the assessee's case insofar as it high-lights the fact ***that expenditure in connection with performance of official duties cannot be treated as a benefit given to the assessee."***

Finally, the Delhi Bench of ITAT held that provision of food to the assessees in the course of performance of official duties is not a perquisite as per Section 17(2) of the Act. Similar to the view taken by the Calcutta HC (Supra).

(*c*) Decision of the Mumbai Bench of ITAT in the case of Daniele Bevilacqua v Second ITO [1991] 39 ITD 362 (Bom):

In this case, the assessee was an employee of Columbia Pictures Industries Inc. USA (USA Company). The USA Company was given distribution right of the film 'Gandhi'. The USA Company had an agent in India namely, Columbia Film of India Ltd. (Indian Company). The Indian company appointed the assessee on payment of monthly salary as well as housing allowance for which an approval of the Reserve Bank of India (RBI) was also obtained. As the assessee was finding the monthly remuneration insufficient, the Indian company agreed to bear all the hotel expenses (boarding, lodging and laundry etc.) of the assessee during his stay in India. For the AY 1983-84, the Indian company paid Rs. 2,45,644 to two hotels viz. Hotel Oberoi and Hotel Feryas. The assessee filed the return of income for AY 1983-84 declaring Nil income since no salary was paid to the assessee. The ITO taxed Rs. 2,45,644 as salary. The assessee preferred an appeal before the CIT(A) and urged that Rs. 2,45,644 was exempt from tax as per Section 10(14) of the Act. However, the CIT(A) upheld the order of the ITO and the assessee preferred a further appeal before the Mumbai Bench of ITAT.

The Mumbai Bench of ITAT held that all the hotel expenses on food, laundry etc. were the personal obligation of the assessee, which was paid by his employer. Thus, Rs. 2,45,644 was nothing but a perquisite as per Section 17(2)(iv) of the Act. Further, the

Mumbai Bench of ITAT outrightly rejected the claim of exemption under Section 10(14) of the Act stating that hotel expenses were incurred at a place where duties of office were ordinarily performed.

In arriving at this conclusion, the Mumbai Bench of ITAT distinguished the decision of the Calcutta HC (Supra) stating that D. S. Blackwood was an employee of foreign company who was deputed to supervise certain erection work in India whereas in the given case, the assessee was an employee of the Indian company. There was no evidence that showed that the assessee was specifically sent to India by the USA Company. In fact, on the contrary, the Indian company had appointed the assessee on its payroll.

Thus, it was in light of these facts coupled with the fact that no salary was paid to the assessee, the Mumbai Bench of ITAT held that value of hotel accommodation provided to the assessee was a perquisite as per Section 17(2)(iv) of the Act.

In our view, in light of the aforesaid decisions, one can argue that the rent-free accommodation/ hotel accommodation provided to the employees who are stranded at a place other than their regular place of employment due to lockdown so that such employees can perform official duties, is not a benefit given by the employer to such employees and accordingly, is not a perquisite as per Section 17(2) of the Act. Consequently, the value of such rent-free accommodation/ hotel accommodation should not be charged to tax as salary.

Please note that the views expressed above are the personal views of the writers. Readers are advised to examine the facts and circumstances of the case and take appropriate professional advice before taking any decision.

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