3.1 Concepts of Tax Planning
3.2 Tax Planning of Employees
3.3 Deductions from Salaries for the AY 2010-'11
3.4 Relief of Tax under Section 89 of the Act
3.5 Rates of Income Tax
3.6 Tax Planning in respect of Tax Deducted at Source

In an organized society, tax is unavoidable because it is the price paid for administrative and political stability by the public to the Government. It is the duty of each citizen to pay due taxes in time and not to resort to any device to evade the payment of taxes. An effective tax strategy is vital for successful financial planning since payment of taxes reduces the disposable income of the tax payers. To solve the problem of tax burden, the concept of tax planning has been introduced in the Income Tax Act. Tax planning may be defined as an arrangement of one’s financial affairs in such a way that without violating in any way the legal provisions, full advantage is taken of all tax exemptions, rebates, allowances and other reliefs or benefits permitted under the Act. This will reduce the burden of taxation on the assessee as far as possible.

Tax planning may be regarded as a method of intelligent application of expert knowledge of planning one’s economic affairs with a view to securing the consciously provided tax benefits on the basis of national priorities in keeping with the legislative and judicial opinion. But it does not imply taking undue advantage of loopholes in tax laws or evading tax liability. Hence tax planning is defined as the methods used by a tax payer to reduce his burden of
taxes in a legal manner. Tax planning may be legitimate provided it is within the framework of tax laws. Hence tax evasion and tax avoidance must be understood as distinct from tax planning.

The present chapter discusses the concepts of tax planning and explains the deductions and relief available to individual income tax assessees under the provisions of the Income Tax Act for the period under study. The chapter is organized into two parts. While the first part explains the concepts of tax planning, second part discusses tax planning of employees under the provisions of Income Tax Act, 1961.

### 3.1 Concepts of Tax Planning

This part of the chapter explains the important concepts of tax planning namely short range and long range tax planning, tax planning and tax laws, tax evasion and tax avoidance and tax management.

#### 3.1.1 Short Range and Long Range Tax Planning

Tax planning may be classified into two broad heads: short range tax planning and long range tax planning. Short range tax planning may be the same as year to year planning to achieve a specific or limited objective. For example, an employee whose income is likely to register an unusual growth in a particular year as compared to the preceding year, might plan to subscribe to the PPF/NSC with in the prescribed limits in order to enjoy substantive tax relief. By investing in such a way, he is not making permanent commitment but he is substantially making savings in the tax. Short term goals for each year should be identified and it should be consistent with the long term goals.

In the case of long range tax planning, each tax payer should identify and specify his long term financial objectives. Long term goals must be flexible
enough to adapt changes as well as strong enough to accommodate short term plans. The long range planning sometimes may not even confer immediate tax benefits. It aims at a long future period, the benefit of which may be spread over a number of years in future. For example, in case where an employee transfers certain shares to his minor son, the income arising from the shares will be clubbed with transferor’s income under section 64 (IA) of the Act.

3.1.2 Tax Planning and Tax Laws

Tax planning involves in every case a thorough and up to date knowledge of tax laws. Tax laws in India are highly complex and difficult to be understood by a common man. The complexity is further increased by frequent amendments made in the tax laws every year. Therefore it becomes necessary to have an up - to - date knowledge not only of the statutory law but also of the judge made laws in the form of various decisions of the Courts. One of the best methods to study tax planning is through the case law. The judgments of the Supreme Court and various High Courts reveal instances of successful and unsuccessful tax planning. The judgments touch up on various provisions of tax laws and their application to different situations. The question of interpretation of law can also have a bearing on the success or failure of tax planning. Moreover, a sound method of tax planning should be carefully planned after considering that whatever is done is not only strictly with in the frame work of law, but is also in consonance with the legislative intentions and should be sensible to any reasonable person.

Interpretations made by one High Court should normally be accepted by other High Courts (CIT vs. Jayantilal Ramenlal & Co. 137 ITR 257, CIT vs. Vrajlal Manilal 127 ITR 512). In view of this position one should realise the importance and usefulness of keeping tract of the judgments of Supreme Court.
and various High Courts as reported in Income Tax Reports from time to time. He should make it a point to go through the relevant cases and understand the issues involved and the rationale of the judgments. In addition, it would do well to keep track of the Circulars issued by the Central Board of Direct Taxes from time to time. These circulars are also published in the Income - Tax Reports and other journals. Moreover, tax payers will also find it profitable to go through the various articles on tax laws published in law journals and financial papers.

3.1.3 Tax Evasion and Tax Avoidance

Each tax payer is expected to make voluntarily disclosures of his income and tax liabilities through legal compliance. When a tax payer deliberately or consciously does not furnish material particulars or furnishes inaccurate or false particulars or defrauds the State by violating any of the legal provisions, it shall be termed as tax evasion. Tax evasion is considered as unethical and illegal. Tax avoidance, on the other hand, is a method of reducing tax liability by availing of certain loopholes and lacunae in the law. It is the art of escaping the burden of tax without breaking the law. However, this kind of tax planning demands a thorough knowledge of the provisions of the tax laws and relevant legal decisions as well as other statutes affecting any aspect of taxation. In this context, it is worth noting that taking advantage of the loopholes in law provides only short run benefits because, as and when the loopholes in the law are made public or sometimes even earlier, legislature steps into plug the loopholes.

In the earlier days, it was established in various courts both in India and abroad that tax avoidance is legally valid. It has been laid down in the case of Ramaswami Naicher vs. State of Madras (1968) 69 ITR 420 that “it is open to the tax payer to avoid tax if he can do so within the limits of the law without
violating it.” In recent years, however, the courts have changed their attitude towards tax avoidance and view tax avoidance with displeasure. The Supreme Court of India in the McDowell Co Ltd. vs. CTO 154 ITR 148 (SC) said that “it is neither fair not desirable to expect the legislature to intervene and take care of every device and scheme to avoid taxation, it is up to the court to determine the nature of new and sophisticated legal devices to avoid tax and consider whether the situation created by the devices for what they really are and to refuse to give judicial benediction”. In the same judgment, Supreme Court judges made a clear distinction between tax avoidance and tax planning - tax planning may be legitimate provided it is with in the frame work of law. Colorable devices cannot be part of tax planning and it is wrong to encourage or entertain the belief that it is honorable to avoid the payment of tax by resorting to dubious methods. It is the obligation of every citizen to pay the taxes honestly without resorting to subterfuges.” It is clear from the above judgment that what constitutes a crime is tax evasion and what is undesirable is tax avoidance but it is certainly desirable to engage in the practice of tax planning. However, there is a thin line of demarcation between tax avoidance and tax evasion. Therefore it is said that a successful tax evasion becomes legitimate avoidance, while unsuccessful avoidance may be treated as tax evasion.

3.1.4 Tax Management

Tax planning is a wider term and it includes tax management also. Tax management is an important aspect of tax planning. Planning which leads to filing of various returns in time, compliance of the applicable provisions of law and avoiding of levy of interest and penalties can be termed as efficient tax management. It is an exercise by which defaults are avoided and legal compliance is secured. The filing of returns with all proper documentary evidence for the various claims, rebates, reliefs, deductions and computation of
income and tax liability would come under the purview of tax management. The assessee is exposed to certain unpleasant consequences if obligations cast under the tax laws are not duly discharged. Such consequences take shape of levy of interest, penalty, prosecutions, forfeiture of certain rights etc. Therefore any effort in tax planning is incomplete unless proper discharge of responsibilities is made. Tax management includes:

- Compiling and preserving data and supporting documents evidencing transactions, claims etc.
- Making timely payment of taxes.
- TDS and TCS compliance.
- Following procedural requirements.
- Timely filing of returns.
- Responding to notices received from the authorities.
- Preserving record for the prescribed number of years.
- Mentioning PAN, TAN etc. at appropriate places.

3.2 Tax Planning of Employees

In the matter of taxation of salaries, the law of income tax has recently been made comprehensive. Almost every type of salary, or remuneration of every kind of employee, government or private, is covered under it. Therefore, it becomes very important for an employee; however high or low placed he may be, to understand at least those fundamental principles of income - tax law which directly or indirectly affect him, before he is caught unaware in the net of taxation. Employees, next to the business community, constitute the biggest sector of income tax paying public and contribute the most to the income tax in
the country. Since income from salary has been accounted correctly and there is less or no scope for evasion, this class of tax payers is considered as the most honest in the records of Income Tax Department.

However, in a period of ever growing inflation resulting in spiraling prices, it is the fixed income earners who suffer the most. The salaried tax-payers are the hardest hit in every case where there is a serious economic crisis in the country leading to uncontrolled rise in prices without a corresponding increase in the volume of goods that are available for consumption. In view of the constant erosion in the intrinsic value of the rupee, the fixed income groups are left with no choice but to forego a major part of the conveniences and benefits, which they would otherwise have availed of. In a constant effort to match income and expenditure and to see that the family budget is kept at safe levels, each tax-payer in the salaried group is required or even forced to put in more serious effort than tax-payers carrying on business or others who are in the fluctuating income group.

In view of this, tax planning is of great importance to every employee because it leaves the maximum possible amount of salary after payment of taxes with them. This could be achieved only by availing maximum amount of tax exemptions, deductions and relief. Therefore, tax planning is the scientific planning made by the employees to attract minimum liability to tax and or postponement of the tax liability for the subsequent period by availing of various incentives, concessions, allowances, rebates and relief provided, in the context of existing tax laws.

While planning for salary income, the following hints will be of much use to the employees in getting maximum benefits of tax planning.
Tax on salaries can be reduced to minimum if salary is divided into different allowances (which are not taxable or which are partially exempt from tax) and perquisites.

It should be ensured that, under the terms of employment, dearness allowance and dearness pay form part of basic salary. This will minimise tax incidence on house rent allowance, entertainment allowance, gratuity and commuted pension.

A tax-payer should properly assess the incidence of tax and choose between going in for house rent allowance or rent free furnished or unfurnished accommodation. House rent allowance is exempt under section 10 (13A) of the Income Tax Act within the limits prescribed by Rule 2A of the Income Tax Rules, 1962.

There are several employees’ welfare schemes such as recognised provident fund, approved superannuation fund, gratuity fund etc. Payments received from such funds by the employees are totally exempt or exempt up to significant amounts.

Employees should go in for free medical facilities instead of a fixed medical allowance, since medical allowance is taxable.

Reimbursement of expenditure on medical treatment of the employee or his family members is exempted up to ₹ 15000.

Travel concession should be claimed to the maximum possible extent without attracting any incidence of tax.

Avail deductions under Section 80C of the Income Tax Act to the maximum possible extent.
• Encashment of earned leave on retirement of employees is exempted fully/partially, as the case may be. Leave encashment while in service is treated as part of salary.

• Leave Travel Concession (LTC) or Leave Travel Allowance (LTA) is allowed twice in a block of four years. The allowance is exempt subject to amount of expenses actually incurred by the employee for such travel.

• An employee should take the benefit available under section 89(1) of the Income Tax Act when salary is received in arrear or advance.

• As uncommuted pension is always taxable, employees should get their pension commuted. Commuted pension is fully exempt from tax in the case of Government employees and partially exempt from tax in the case of non-govt. employees who can claim relief u/s 89 (1) of the Income Tax Act.

• Since incidence of tax on retirement benefits like gratuity, commuted pension, accumulated balance of unrecognised provident fund is lower if they are paid in the beginning of the financial year, employers and employees should mutually plan their affairs in such a way that retirement, termination or resignation, as the case may be, takes place in the beginning of the financial year.

• VRS is exempt up to five lakh rupees if VRS is as per prescribed conditions.

**3.3 Deductions from Salaries for the AY 2010 - ‘11**

Income Tax Act, 1961 provides various types of deductions and allowances to the employees from time to time. Income chargeable under the head “Salaries” shall be computed after allowing these deductions. A scientific tax planning will be of much helpful to the employees in availing of these benefits to the maximum
possible extent and thereby reducing the incidence of tax. A brief discussion about the deductions available under Section 16, Section 24, Chapter VI-A and relief of tax under Section 89 of the Income Tax Act is made here in.

3.3.1 Deductions under Section 16

Standard deduction under Section 16(i) was available to all employees up to Assessment Year 2005 - ‘06. This deduction has been withdrawn w.e.f. AY 2006 – ‘07. At present there are two deductions available under Section 16. They are entertainment allowance under Section 16(ii) and tax on employment under Section 16(iii).

3.3.2 Entertainment Allowance - Section 16(ii)

This deduction is allowed only to Government employees. Non-Government employees shall not be eligible for any deduction on account of any entertainment allowance received by them. In the case of entertainment allowance, the assessee is not entitled to any exemption but he is entitled to a deduction under Section 16(ii) from gross salary. Therefore, the entire entertainment allowance received by an employee is added in computation of the gross salary. The Government employee is, then, entitled to deduction from gross salary on account of such entertainment allowance to the extent of minimum of the following three limits.

1. Actual entertainment allowance received during the previous year.
2. Twenty per cent of his salary exclusive of any allowance, benefit or other perquisite.
3. ₹ 5,000.
3.3.3 Tax on Employment - Section 16(iii)

As per the Constitution of India, the State Government or Local Authorities are empowered to make law and to collect taxes on professions. However, the total amount payable in respect of any one person shall not exceed ₹ 2,500 per annum. As per Section 16(iii), any sum paid by the assessee on account of tax on employment shall be allowed as a deduction in the year in which the tax is actually paid.

3.3.4 Deduction in respect of Interest on Housing Loan (Section24B)

Loss under the head “Income from House Property” being interest on house loan may be claimed as a deduction under Section 24B of the Income Tax Act. It allows an assessee to deduct interest payable on the borrowed capital of self occupied house property, where such property has been acquired, constructed, repaired, renewed or reconstructed with borrowed capital. The amount of interest payable yearly should be calculated separately and claimed as a deduction every year. It is immaterial whether the interest has been actually paid or not paid during the year. The maximum amount of interest eligible for such deduction is ₹ 30,000 for housing loan taken for construction or acquisition of residential building up to 31st March, 1999. Where the property is acquired or constructed with capital borrowed on or after 1st April, 1999 and such acquisition or construction is completed within three years of the end of the financial year in which the capital was borrowed, actual interest payable subject to a maximum of ₹ 150,000 is allowed as a deduction. The higher rate is not allowed for loans taken for repairs/renovation.

3.3.5 Deductions under Chapter-VI-A

In computing the total income of an assessee, certain deductions are permissible under Chapter VIA of the Income Tax Act, from the gross total income. These deductions are available in the form of tax free investments and
deductions in respect of certain expenditures incurred by the assessee towards medical treatment, higher education etc for the relevant financial year. They include deductions under Section 80C to 80U of the Act. Section 80C covers deductions on account of payments and or investments made in specified investment avenues. Section 80CCC and 80CCD cover contribution towards approved pension funds. The aggregate of deductions under Section 80C, 80CCC and 80CCD shall not exceed ₹ 1 lakh. Table 3.1 presents important deductions under Chapter VIA of the Income Tax Act for the AY 2010-11.

Table 3.1 Deductions under Chapter - VI - A for AY 2010-11

<table>
<thead>
<tr>
<th>Sl. No.</th>
<th>I-T Section</th>
<th>Category</th>
<th>Amount of Deduction</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>80C</td>
<td>Aggregate of amount paid/incurred/invested towards any of the following:</td>
<td>Up to ₹ 1 Lakh.</td>
</tr>
<tr>
<td></td>
<td></td>
<td>a. Premium paid towards life Insurance Policy not exceeding 20% of the total sum assured.</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>b. Any annuity or Deferred Annuity Plan</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>c. Contribution towards approved PF including PPF</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>d. Subscription towards NSC</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>e. Contribution to UTIs Retirement Benefit Plan</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>f. Investment in UTIs Unit Linked Insurance Plan</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>g. Approved Mutual Fund Investment</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>h. Repayment of housing loan- principal amount- towards self-occupied residential property</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>i. Payment of tuition fees towards any two children of the assessee</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>j. Investment in Equity Linked Savings Scheme/Approved Infrastructure Bonds</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>k. Investment in Pension Fund/Deposit Scheme of National Housing Bank under Home Loan Account Scheme</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>l. Fixed Deposit of any Scheduled bank/Housing Finance Corporation for not less than 5 years</td>
<td></td>
</tr>
<tr>
<td>Column</td>
<td>Code</td>
<td>Description</td>
<td></td>
</tr>
<tr>
<td>--------</td>
<td>------</td>
<td>-------------</td>
<td></td>
</tr>
<tr>
<td>m.</td>
<td>80CCC</td>
<td>Investments in Equity Shares/Debentures of approved public financial institutions or Companies.</td>
<td></td>
</tr>
<tr>
<td>80CCD</td>
<td>3</td>
<td>Premium paid towards IRDA approved Pension Fund Up to ₹ 1 Lakh.</td>
<td></td>
</tr>
<tr>
<td>a.</td>
<td>Amount paid / deposited in an approved Pension Scheme of Central Govt. Up to 10% of salary</td>
<td></td>
<td></td>
</tr>
<tr>
<td>b.</td>
<td>Matching contribution made by the employer to the Pension account of Individual Upto10% of salary</td>
<td></td>
<td></td>
</tr>
<tr>
<td>80 CCE</td>
<td>4</td>
<td>Aggregate of Deduction u/s 80C, 80CCC &amp; 80CCD Not exceeding ₹ 1 Lakh</td>
<td></td>
</tr>
<tr>
<td>a.</td>
<td>Medical Insurance Premium paid by any mode other than cash. Up to ₹ 15,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>b.</td>
<td>For senior citizens Up to ₹ 20,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>80DD</td>
<td>6</td>
<td>a. Any expenditure for Medical, Nursing and Rehabilitation incurred on dependent relative suffering from Permanent Physical Disability, Autism, Cerebral Palsy and Multiple Disability. Up to ₹ 50,000 if disability is over 40% and ₹ 75,000 if disability is over 80%.</td>
<td></td>
</tr>
<tr>
<td>b.</td>
<td>Deposit under LIC, UTIs Scheme and other IRDA approved insurers for the benefit of physically handicapped dependent.</td>
<td></td>
<td></td>
</tr>
<tr>
<td>80DDB</td>
<td>7</td>
<td>a. Actual expenditure incurred on medical treatment of self, or dependent relative suffering from terminal diseases like Cancer, AIDS, Renal Failure etc. Up to ₹ 40,000</td>
<td></td>
</tr>
<tr>
<td>b.</td>
<td>For Senior Citizens Up to ₹ 60,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>80E</td>
<td>8</td>
<td>Interest on repayment of loan taken from charitable/financial institution for self, spouse, children higher education for a maximum of 8 years. Any amount of interest.</td>
<td></td>
</tr>
<tr>
<td>80G</td>
<td>9</td>
<td>a. Donation paid to Prime Minister’s Relief Fund, National Defense Fund, Funds of Universities or Educational Institution of national fame, National Trust for welfare of persons with Autism, Cerebral Palsy, Mental Retardation and multiple disabilities. Amount varies as per the nature of the fund or donee institution specified in the Act.</td>
<td></td>
</tr>
</tbody>
</table>
### b. Donation to National Children’s Fund, Jawaharlal Nehru Memorial Fund, PMs Drought Relief Fund, any Charitable or Religious Institutions, Corporation established for promoting interest of the members of a minor community

<table>
<thead>
<tr>
<th>10</th>
<th>80GG</th>
<th>Deduction in respect of rent paid, provided no house is owned by self, spouse or minor child in the place of work and residing in any of the specified cities.</th>
<th>Lowest of actual amount of HRA received or ₹ 2,000 per month or rent paid in excess of 10% of total income subject to a ceiling of 25% thereof.</th>
</tr>
</thead>
<tbody>
<tr>
<td>11</td>
<td>80U</td>
<td>Persons suffering from permanent physical disability and includes Autism, Cerebral Palsy, Multiple Disability, Person with disability and severe disability.</td>
<td>₹ 50,000 if disability is over 40% and ₹ 75,000 if disability is over 80%.</td>
</tr>
</tbody>
</table>

Source: Finance Act 2005 to 2010

A new section 80CCF has been introduced in the budget 2010 which allows tax free investments in infrastructure bonds of specified institutions to the extend of ₹ 20,000. With effect from AY 2011 - ‘12, the aggregate of deductions available under Section 80CCE and 80CCF will be ₹ 120,000.

### 3.4 Relief of Tax under Section 89 of the Act

If an assessee receives during the previous year any sum as advance salary or as arrear salary in respect of the years preceding the previous year or any other payment from the employer in relation to past services, his tax liability is bound to increase as a result of increase in the taxable income. If it is possible to add such arrear or advance salary to the income of respective years
to which they related, the tax liability of the assessee in respect of the income of the previous year will be reduced considerably. Under Section 89 of the Income Tax Act, relief will be granted to such assessees. The assessee may apply for grant of relief under Section 89(1) in relation to the following taxable amounts.

a. Advance of salary.
b. Arrear of salary.
c. Gratuity-Section 10(10).
d. Commutation of Pension- Section 10(10A).
e. Encashment of earned leave- Section 10(10AA).
f. Retrenchment compensation-Section 10(10B).
g. Profits in lieu of salary- Section17(3)
h. Unrecognised Provident Fund.

No relief shall be granted in respect of any amount received or receivable by an assessee on his voluntary retirement or termination of his service, if an exemption in respect of which has been claimed by the assessee under section 10(10C) in respect of such, or any other, assessment year.

3.5 Rates of Income Tax

In order to compute the tax liability and to arrive at proper decision in the matter of planning, every assessee should know the prevailing tax rates. Every year, the changes in the tax laws will be made available by amendments made in the Finance Act. Table 3.2 presents the tax rates applicable to individual income tax assessees for the AY 2010 - ‘11.
### Table 3.2 Income Tax Rates for the AY 2010-11

<table>
<thead>
<tr>
<th>Taxable Income (₹)</th>
<th>Income Tax Rates for</th>
<th>Primary and Secondary Education Cess</th>
<th>Surcharge</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Male below 65 years</td>
<td>Women below 65 years</td>
<td>Senior Citizens (65 years. and above)</td>
</tr>
<tr>
<td>Up to 160,000</td>
<td>Nil</td>
<td>Nil</td>
<td>Nil</td>
</tr>
<tr>
<td>160,001 to 190,000</td>
<td>10%</td>
<td>Nil</td>
<td>Nil</td>
</tr>
<tr>
<td>190,001 to 240,000</td>
<td>10%</td>
<td>10%</td>
<td>Nil</td>
</tr>
<tr>
<td>240,001 to 300,000</td>
<td>10%</td>
<td>10%</td>
<td>10%</td>
</tr>
<tr>
<td>300,001 to 500,000</td>
<td>20%</td>
<td>20%</td>
<td>20%</td>
</tr>
<tr>
<td>500,001 and above</td>
<td>30%</td>
<td>30%</td>
<td>30%</td>
</tr>
</tbody>
</table>


In the AY 2010-11 the income tax exemption limit applicable to men below 65 years was ₹ 160,000. It was ₹ 190,000 to women below 65 years and ₹ 240,000 to senior citizens. Education cess @ 3 per cent of income tax was levied during this period. However, surcharge on income tax has withdrawn w.e.f. AY 2010-11.

### 3.6 Tax Planning in respect of Tax Deducted at Source

The Income Tax Act 1962 envisages payment of taxes in four different modes. They are:

1. Deduction of tax at source.
2. Advance tax.
3. Self assessment tax and
4. Tax on Demand.

Of the four methods, the most important method as far as salaried assessees are concerned is deduction of tax at source. Section 192 of the Act makes it clear that any person responsible for paying any income chargeable under the head “Salaries” shall at the time of payment, deduct income - tax on the estimated income of the employee under the head “Salaries” for that financial year. The tax is to be deducted at the average of income tax computed on the basis of the rates in force for the financial year in which the payment is made. In other words, the total tax to be deducted, on the estimated income of the employee for the relevant financial year, is divided by the number of months of his employment during the financial year. The amount so arrived at is the monthly deduction of tax at source.

TDS provisions relating to payment of salary are materially different from provisions for other payments, in respect of the manner of determining the amount to be deducted. In respect of all other payments, the person deducting tax has to deduct a fixed percentage of gross amount payable, irrespective of payee’s income tax liability. However, in respect of salary payment, the employer has to make an honest estimate of income under the head salary and deduct tax at the appropriate rate, on the income so estimated. This casts an onerous responsibility on the employer to examine the allowability of various deductions, rebate and relief to the employee under the Income Tax Act, which is normally subject to verification by the Assessing Officer. The employer has to walk on thin ice in the matter of deduction of tax at source from salary, as excess deduction may antagonise the employee and lower deduction may invite penal action from the tax department.
In view of this, tax planning in respect of TDS becomes more important on the part of the employees. Since the monthly tax to be deducted is the average of income tax computed for the relevant financial year, the employee should take care of all the deductions and benefits available under the Act after considering the amendments made in the Finance Act of the respective year. He has to plan his savings and investments in advance so that one could avail the maximum possible benefits available under the Act. Thus it is clear that tax planning is a matter which is to be formulated in the beginning of the financial year itself so that monthly tax deducted at source will be adequate, not resulting in excess or short deduction.

This chapter discussed the important concepts of tax planning and the deductions from salaries under the provisions of the Income Tax Act which are generally applicable to salaried income tax assessees. It provides a theoretical framework to the current study. It is evident from the above discussion that tax planning is of utmost importance to salaried class income tax assessees in view of their stabilised income and strict obligations to tax compliance. It also reveals that tax laws in India are subject to frequent changes and such amendments would have some positive as well as negative impact on the tax liability of the employees. The review of literature also stated that the tax reforms in India were made mostly on an ad-hoc basis without adequate examination of the total impact on various aspects of taxation. In view of this, the following chapter will make an attempt to study the personal income tax reforms in India during the post liberalisation period and analyzing its impact on the salaried income tax assessees.