



No income tax on salary recovered for not serving notice period

Background

Recently, the Ahmedabad Bench of the Income-tax Appellate Tribunal (the Tribunal) in the case of Nandinho Rebello¹ (the taxpayer) inter alia held that only the actual salary received by the taxpayer post the deduction of notice pay by the employer as per the terms of the employment agreement is taxable. In other words, deduction made by the employer for not serving the notice period need not be considered as taxable salary and brought into the purview of income tax.

Facts of the case

- The Assessing Officer (AO) during the course of re-assessment proceedings² observed that the taxpayer has worked with three employers during the Assessment Year (AY) 2010-11 and had not disclosed his salary received from two of the three employers. The AO passed an order³ bringing such income to tax, without considering the deduction of notice pay recovery made by the said two employers.
- The taxpayer preferred an appeal before the Commissioner of Income-tax (Appeals) [CIT(A)] against the order passed by the AO.

¹ Nandinho Rebello v. DCIT (ITA No. 2378/Ahd/2013)

² Under Section 148 of the Act

³ Under Section 143(3) read with Section 147 of the Act

- The CIT(A) upon hearing the submission of the taxpayer, sustained the additions made by the AO on the following grounds:
 - Income under the head salary is computed in accordance with the provisions⁴ of the Income-tax Act, 1961 (the Act).
 - The AO has charged salary to income tax on a due basis.
 - The deduction made by the employer for the notice period is not provided in the Act⁵.
 - The taxpayer's argument of the taxability of real income is not tenable as the doctrine of real income is not applicable and the provisions⁶ of the Act imposes the charge when salary becomes due.
 - The CIT(A) held that the decision relied upon by the taxpayer⁷ was not relevant and instead relied upon a judicial precedent⁸ where remuneration accrued to the taxpayer was brought to tax despite being waived.
- The taxpayer filed an appeal before the Tribunal against the orders passed by the CIT(A).

⁴ Sections 15 to 17 of the Act

⁵ Section 16 of the Act - Deductions available under the head 'Salary'

⁶ Section 15 of the Act

⁷ Ramchandra Dhonde Datar v. CIT [1961] 43 ITR 22 (Bom) dealing with taxability of compensation on termination of employment

⁸ CIT v. P. Natraja Shastri [1976] 104 ITR 295 (Mad)

Tribunal's decision

- The employers had made a recovery from the salary paid to the taxpayer for not serving the notice period as per the terms of the employment agreement with the respective employers.
- The provisions⁹ of the Act need not be referred to in this instance, as it is a case of recovery of salary and not a deduction.
- Only the actual salary received by the taxpayer would be taxable since the amount received by the taxpayer is after the recovery of the notice period as per the employment agreement.
- Under these circumstances, the addition of notice pay period was deleted.

Our comments

This decision differentiates between actual salary received and income on a due basis. This judgment could support cases where notice pay is contractually recovered from employees. However, it is important that the said recovery be in accordance with the terms of the employment agreement. Considering the Act does not explicitly provide for such a recovery, litigation cannot be ruled out.

⁹ Section 16 of the Act



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