Note regarding valuation of perquisite in respect of housing accommodation provided by an employer to its employees

Recently, the Supreme Court has rendered a very important judgement in respect of valuation of perquisite regarding housing accommodation provided by an employer to its employees, in the case of *Arun Kumar and Others Vs. Union of India [2006] 286 ITR 89 (S.C.).* In this case, the validity of rule 3 of Income-Tax Rules, 1962(the Rules), as amended in 2001, was challenged before the Apex Court. Though the Apex Court has upheld the validity of the aforesaid rule 3, but it has laid down some very significant principles in this regard in the light of the provisions of section 17(2)(ii) of the Income-Tax Act, 1961 (the Act).

Before we proceed further in this regard, it would be appropriate to understand the relevant provisions of the Act and the Rules, which are discussed, as follows:-

1. Section 17(2) of the Act defines the term '*perquisite*' and as per section 17(2)(ii) of the Act, '*perquisite*' includes the value of any concession in the matter of rent respecting any accommodation provided to the assessee by his employer, and

2. As per rule 3 of the Rules [as amended with effect from 1.4.2005], where the accommodation is provided by an employer other than the Central or State Government, the aforesaid perquisite shall be evaluated as follows:

   (a) Where the accommodation is owned by the employer-

      (i) 20% of salary in cities having population exceeding four lakhs as per 2001 census.

      (ii) 15% of salary in other cities

      – as reduced by the rent, if any, actually paid by the employee.

   (b) Where the accommodation is taken on lease or rent by the employer-

      Actual amount of lease rental paid or payable by the employer or 20% of salary whichever is lower, as reduced by rent, if any, actually paid by the employee.

      [The aforesaid percentages before 1.4.2005 and with effect from 1.4.2001, were 10 & 7.5 in place of 20 and 15, respectively]

We will now discuss the aforesaid judgement of the Supreme Court. In order to keep this discussion brief, the relevant parts of the head-note on pages 89, 90, 91 and 92 of the Report are reproduced as follows:-

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(i) *Though rule 3 of the Income-tax Rules, 1962, as amended in 2001, cannot be held arbitrary, discriminatory or ultra vires article 14 of the Constitution of India or inconsistent with section 17(2)(ii) of the Income-tax Act, 1961, it is in the nature of a "machinery provision" and applies only to cases of "concession" in the matter of rent respecting any housing accommodation provided by an employer to his employees. Whether or not Parliament could have in the exercise of legislative power created a "deeming fiction" as to concession in the matter of rent in certain circumstances, no such deeming provision is found in the Act. It is, therefore, open to the assessee to contend that there is no "concession" in the matter of accommodation provided by the employer to the employees and the case is not covered by section 17(2)(ii).*

Rule 3, even after amendment in 2001, would apply only to those cases where "concession" has been shown by an employer in favour of an employee in the matter of rent respecting accommodation. Thus, whereas the "charging provision" is found in the Act of Parliament [section 17(2)(ii)],the "machinery component" is in the subordinate legislation (rule 3). The latter will apply only after liability is created under the former. Unless the liability arises under section 17(2)(ii) of the Act, rule 3 has no application and the method of valuation for calculating concessional benefits cannot be resorted to.

Prior to its amendment in 2001 rule 3 was totally different. It dealt with the method of calculation of the concession keeping in view the concept of "fair rental value". In the light of the principle and phraseology in rule 3,the rule making authority provided an opportunity to the assessee to satisfy the Assessing Officer that the rent sought to be recovered from the employee could not be said to be a "concession" as it was "fair rent", "reasonable rent", "market rent" or "standard rent".

After the 2001 amendment of rule 3, there is no scope for determination of fair rental value. The concept of fair rental value either on the basis of the normal rent or on the basis of the market rent available in the locality or on the basis of the municipal valuation has been done away with. When the concept of "fair rent", "market rent", "reasonable rent" or "standard rent" is no more relevant or germane in deciding the question, it was open to the Legislature to empower the rule making authority to provide the method for calculation of a "concession".

The criterion which was adopted by the rule-making authority in treating cities having population of less than four lakhs and more than four lakhs cannot be said to be arbitrary or unreasonable and fixation of rent on the basis of population of the city cannot be interfered with in exercise power of judicial review.

*A "perquisite" is a privilege, gain or profit incidental to an employment in addition to regular salary or wages. It is a benefit or an advantage received by the holder of an office over and above his salary. The benefit received by an employee is incidental to employment in excess of or in addition to the salary-.***Owen v. Pook (Inspector of Taxes) [1969] 74 ITR 147 (HL)** *relied on.*

In computing a perquisite in the matter of residential accommodation, the fundamental question of applicability of section 17(2) of the Act still remains. It cannot be gainsaid that section 17(2) would apply only if there is a "perquisite". Indisputably, the definition of "perquisite" is inclusive in nature and takes within its sweep several matters enumerated in clauses (i) to (vii). Section 17(2)(ii) declares that the value of any "concession" in the matter of rent respecting any accommodation provided to the employee by his employer would be a "perquisite". Nevertheless, it must be a "concession" in the matter of rent respecting any accommodation provided by the employer to his employee. It is, therefore, clear that before section 17(2)(ii) can be invoked or pressed into service and before calculation of concession as per rule 3, even after its amendment in 2001, is made, the authority exercising power must come to a positive conclusion that it is a concession. The "concession" is, thus, a foundational, fundamental or jurisdictional fact.

(ii) "Concession" under sub-clause (ii) of clause (2) of section 17 of the Act is a "Jurisdictional fact". It is only when there is a "concession" in the matter of rent respecting any accommodation provided by an employer to his employee that the mode, method or manner as to how such concession can be computed arises. In other words, concession is a "jurisdictional fact"; the method of fixation of the amount is a "fact in issue" or an "adjudicatory fact". If the assessee contends that there is no "concession", the authority has to decide the said question and record a finding as to whether there is "concession" and the case is covered by section 17(2)(ii). Only thereafter may the authority proceed to calculate the liability of the assessee under the Rules.

Section 17(2)(ii) does not contain any "deeming clause" that once it is established that an employee is paying rent less than 10 per cent of his salary in cities having a population of four lakhs or 7.5 per cent in other cities, it should be deemed to be a "concession" within the meaning of the Act and such employee must be deemed to receive a "concession" in the form of "perquisite" in the payment of

rent. An employer may provide residential accommodation to his employees for several reasons. It is also possible that for making available staff quarters / colonies / accommodations, State Governments or the Central Government may provide land to public sector undertakings / companies / corporations at a concessional rate imposing appropriate conditions including the amount of rent, if any, to be recovered by the employer. A benefit or facility which furthers the commercial interest of the employer would not per se become a perquisite. Such facility of accommodation furthers the commercial interest of the employer by having a satisfactory work force which but for such accommodation, would not have been available. In such cases, e.g., doctors / superintendents / rectors / professors / teachers / Grihpatis / Grihmatas, etc., to stay in the accommodation provided by the employer may be more a "compulsion" than a "concession".

In this context, we may also refer to the judgement in the case of *Officers Association, Bhilai Steel Plant Vs. Union of India [1983] 139 ITR 937 (M.P.)*, which has been referred to by the Supreme Court in its aforesaid judgement on pages 106 and 107 of the Report. In this connection, the relevant part of the observations of the Supreme Court on page 107 of the Report is reproduced as follows:-

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The court went on to consider that the question was whether an employee was in occupation of an accommodation at a concessional rate, that is, whether the employee had received any concession which could be termed a "perquisite" and gave the answer that it would depend upon two factors: (i) the normal rent for accommodation in occupation of the employee; and (ii) the rent actually paid by the employee. If the rent paid by the employee is the normal rent of the accommodation in his occupation, it cannot be said that he is receiving any concession in the matter of rent even though the rent paid by him is less than 10 per cent of his salary.

In this context, the concluding part of the aforesaid judgement of the Supreme Court is also relevant which is to be found on pages 125 and 126 of the Report. The same is reproduced as follows:-

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For the foregoing reasons, we hold that though rule 3 of the rules cannot be held arbitrary, discriminatory or ultra vires article14 of the Constitution nor inconsistent with the parent Act [section 17(2)(ii)], it is in the nature of a "machinery provision" and applies only to the cases of "concession" in the matter of rent respecting any accommodation provided by an employer to his employees. Whether or not Parliament could have in the exercise of legislative power created a "deeming fiction" as to concession in the matter of rent in certain circumstances (for which we express no final opinion), no such deeming provision is found in the Act. It is, therefore, open to the assessee to contend that there is no "concession" in the matter of accommodation provided by the employer to the employees and the case is not covered by section 17(2)(ii) of the Act.

In the light of the aforesaid discussion, it may be concluded that it is now open to the assessee to contend that there is no '*concession*' in the matter of accommodation provided by the employer to the employees and the case is not covered by section 17(2) (ii) of the Act. This is so even after the amendment of rule 3 in 2001 and 2005, as rule 3 will apply only after liability is created under section 17(2)(ii). Unless the liability arises under section 17(2)(ii) of the Act, rule 3 has no application and the method of valuation for calculating the concessional benefits cannot be resorted to.

Though the Supreme Court has not said so in so many words, the implication of the aforesaid judgement would that the '*fair rent*', '*market rent*', '*reasonable rent*', or '*standard rent*' of the accommodation will have to be considered in order to arrive at a conclusion that there is a '*concession*' in the matter of accommodation provided by the employer to the employees and the case is covered by section 17(2)(ii) of the Act.

The aforesaid judgement of the Supreme Court may be made use of, for the benefit of the employees who have been provided accommodation owned by the employer.

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