

Income Tax Law and Practice

DEBSL301

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LOVELY
PROFESSIONAL
UNIVERSITY



Income Tax Law and Practice

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Content

Unit 1:	Introduction to Basic Concepts of Income Tax Law	1
	<i>Dr. Rupinder Katoch, Lovely Professional University</i>	
Unit 2:	Identification of Residential Status	18
	<i>Dr. Rupinder Katoch, Lovely Professional University</i>	
Unit 3:	Identification of Residential Status	37
	<i>Dr. Rupinder Katoch, Lovely Professional University</i>	
Unit 4:	Computation of Income under the Head Salaries	50
	<i>Dr. Rupinder Katoch, Lovely Professional University</i>	
Unit 5:	Computation of Income under the Head House Property	71
	<i>Dr. Rupinder Katoch, Lovely Professional University</i>	
Unit 6:	Computation of Income under the Head Capital Gains	88
	<i>Dr. Rupinder Katoch, Lovely Professional University</i>	
Unit 7:	Computation of Income under the Head Business & Profession	107
	<i>Dr. Rupinder Katoch, Lovely Professional University</i>	
Unit 8:	Provisions of Depreciation	127
	<i>Dr. Rupinder Katoch, Lovely Professional University</i>	
Unit 9:	Computation of Income from Other Sources	151
	<i>Dr. Rupinder Katoch, Lovely Professional University</i>	
Unit 10:	Clubbing of Income	169
	<i>Dr. Rupinder Katoch, Lovely Professional University</i>	
Unit 11:	Set-off Inter Head Provisions, Set-off Intra Head Provisions	184
	<i>Dr. Rupinder Katoch, Lovely Professional University</i>	
Unit 12:	Deductions from Total Income Law	200
	<i>Dr. Rupinder Katoch, Lovely Professional University</i>	
Unit 13:	Assessment of individuals	214
	<i>Dr. Rupinder Katoch, Lovely Professional University</i>	
Unit 14:	Introduction to Basic Concepts of Income Tax Law	233
	<i>Dr. Rupinder Katoch, Lovely Professional University</i>	

Unit 01: Introduction to Basic Concepts of Income Tax Law

CONTENTS

Objectives

Introduction

- 1.1 Income [Section 2(24)]
- 1.2 Definition of Agricultural Income [Section 2(1A)]
- 1.3 Rule 7- Income from Growing and Manufacturing of any Product
- 1.4 Examples of Agricultural Income
- 1.5 Non-Agricultural Income
- 1.6 Assessee [Section 2(7)]
- 1.7 Person [Section 2(31)]
- 1.8 Basic Principles for Charging Income Tax [Sec. 4]
- 1.9 Classification of Income Earned
- 1.10 Computation of Gross Total Income

Summary

Keywords

Self Assessment

Answers for Self Assessment

Review Questions

Further Readings

Objectives

After studying this unit, you will be able to:

- Comprehend the meaning of “income” used in the Income tax Act, 1961,
- Understand the meaning and scope of agricultural income and use it to determine whether a specific income falls within the scope of agricultural income for the reasons of the section 10(1) exemption,
- Understand the concept of person and assesses,
- Recognize the previous year and assessment year for the purpose of computing income chargeable to tax under the Income-tax Act, 1961,
- Comprehend the procedure for computation of total income for the purpose of levy of income-tax.

Introduction

According to the Indian Constitution, the central government has the authority to impose income taxes. The Income Tax Act, 1961 was consequently passed by the Central Government. The Act outlines the parameters and procedures for income tax collection in India. The Income Tax Rules of 1961, together with a number of additional auxiliary regulations, support the Act. Additionally, the Central Board of Direct Taxes (CBDT) and occasionally the Ministry of Finance, Government of India, release circulars and notifications addressing various areas of the collection of income tax. If a section is not specifically mentioned, the Income Tax Act of 1961's sections will be referred to. Income tax is a charge made at the rates outlined in the applicable Finance Act on the total income

of a person known as the assessee for the prior year that was pertinent to the assessment year. In this part, several of the crucial definitions of the Income Tax Act of 1961 are presented.

1.1 Income [Section 2(24)]

The following receipts are currently specifically counted as income:

- Profits and gains;
- Dividends;
- Voluntary contributions received by a trust/institution;
- The value of any perquisite or profit in lieu of salary taxable under section 17(2)/(3);
- Any special allowance or benefit, other than the perquisite included above;
- Any allowance granted to the assessee to meet his personal expenses at the place where the duties of his office or employment of profit are ordinarily performed by him or at a place where he ordinarily resides or to compensate him for the increased cost of living;
- The value of any benefit or perquisite whether convertible into money or not, obtained from a company either by a director or by a person who has a substantial interest in the company or by a relative of the director or such person and any sum paid by any such company in respect of any obligation which, but for such payment would have been payable by the director or other person aforesaid;
- The value of any benefit or perquisite, whether convertible into money or not, which is obtained by any representative.
- Deemed profits chargeable to tax under section 41 or section 59;
- Profits and gains of business or profession chargeable to tax under section 28;
- Any capital gains chargeable under section 45;
- The profits and gains of any insurance business carried on by Mutual Insurance Company or by a cooperative society;
- The profits and gains of any banking business (including providing credit facilities) carried on by a co-operative society with its members.
- Any winnings from lotteries, crossword puzzles, races including horse races, card games and other games of any sort or from gambling, or betting of any form or nature whatsoever
- Any sum received by the assessee from his employees as contributions to any provident fund (PF) or superannuation fund or Employees State Insurance Fund (ESI) or any other fund for the welfare of such employees;
- Any sum received under a Keyman insurance policy
- Any sum referred to in section 28(va).
- Fair market value of inventory which is converted into, or treated as a capital asset [Section 28(iva)];
- Any consideration received for issue of shares as exceeds the fair market value of the shares [Section 56(2)(viiib)];
- Any sum of money received as advance, if such sum is forfeited consequent to failure of negotiation for transfer of a capital asset [Section 56(2)(ix)];
- Any sum of money or value of property received without consideration or for inadequate consideration by any person [Section 56(2)(x)];
- Any compensation or other payment, due to or received by any person, in connection with termination of his employment or the modification of the term and conditions relating thereto [Section 56(2)(xi)];

Unit 01: Introduction to Basic Concepts of Income Tax Law

- Assistance in the form of a subsidy or grant or cash incentive or duty drawback or waiver or concession or reimbursement, by whatever name called, by the Central Government or a State Government or any authority or body or agency in cash or kind to the assessee is included in the definition of income.
- Any sum referred to in section 28(va).
- Thus, any sum, whether received or receivable in cash or kind, under an agreement for not carrying out any activity in relation to any business or profession or not sharing any know-how, patent, copy right, trade-mark, license, franchise, or any other business or commercial right of a similar nature, or information or technique likely to assist in the manufacture or processing of goods or provision of services, shall be chargeable to income tax under the head “profits and gains of business or profession”;

Concept of Income under The Income-tax Act, 1961

- Regular receipt vis-a-vis casual receipt
- Revenue receipt vis-a-vis Capital receipt
 - Capital gains are not revenue receipts.
 - Capital receipts cannot be taxed, unless they fall within the scope of the definition of “income”
 - Capital receipts which have been specifically included in the definition of income
 - Compensation for modification or termination of services,
 - Income by way of capital gains etc.
- Net receipt vis-a-vis Gross receipt
- Due basis vis-a-vis receipt basis

Broad Principles To Understand Concept of Income

- Income may be received in cash or in kind.
- Income may be from a temporary source or from a permanent source
- A capital receipt is not liable to tax, unless specifically provided in the Act, whereas, a revenue receipt is not exempted, unless specifically provided in the Act.
- Income also includes negative income
- In case of income under the head “Profits & gains of business or profession” and “Income from other sources” (other than Dividend) income shall be taxable on cash or accrual basis as per the method of accountancy regularly followed by the assessee
- A person cannot make profit out of transaction with himself.
- In case of dispute regarding the title of income, normally, be taxed in the hands of recipient
- There is no difference between income received in lump sum or in installment.
- Mere reimbursement of expenses is not an income.
- No difference between legal or illegal income.
- Same income cannot be taxed twice
- In case of mutual activities, where some people contribute to the common fund and are entitled to participate in the fund and the surplus arises which is distributed among the contributors of the fund, such surplus cannot be termed as income.
- Pin money is not treated as income.
- Money embezzled falls within the wider definition of income
- A contingent or anticipated income is not taxable.

- Award received, by a person related to his business or profession, shall be treated as income incidental to such business or profession.

1.2 Definition of Agricultural Income [Section 2(1A)]

- It may be rent or revenue derived from land situated in India and used for agricultural purposes.
- It may be income derived from such land by
 - Agriculture or
 - The performance of a process ordinarily employed by a cultivator or receiver of rent in kind to render the produce fit to be taken to the market or
- The sale, by a cultivator or receiver of rent in kind, of such agricultural produce raised or received by him, in respect of which no process has been performed other than a process of the nature mentioned in point above.
- Lastly, agricultural income may be derived from any farm building required for agricultural operations

Rent or Revenue Derived from Land Situated in India and Used for Agricultural Purposes:

Three conditions:

- a. Rent or revenue should be derived from land;
- b. Land has to be situated in India (If agricultural land is situated in a foreign country, the entire income would be taxable); and
- c. Land should be used for agricultural purposes.

Income Derived from such Land by Agriculture

- "Agriculture" involves basic operations and subsequent operations
- Cultivation of a field involving human skill and labor on the land can be broadly termed as agriculture

Type of Operations:

- Basic Operation: absolutely necessary for the purpose of effectively raising produce from the land are the basic operations
- Subsequent Operations: Operations to be performed after the produce sprouts from the land (e.g., weeding, digging etc.)

Process ordinarily employed to render the produce fit to be taken to the market

- The income from the process employed to render the produce fit to be taken to the market would be agricultural income.
- It must be a process ordinarily employed by the cultivator or receiver of rent in kind and the process must be applied to make the produce fit to be taken to the market.
- If marketing process is performed on a produce which can be sold in its raw form, income derived therefrom is partly agricultural income and partly business income

1.3 Rule 7- Income from Growing and Manufacturing of any Product

- Income is partially agricultural income and partially income chargeable to income-tax as business income,
- The market value of any agricultural produce which has been raised by the assessee or received by him as rent in kind and which has been utilized as raw material in such business or the sale receipts of which are included in the accounts of the business shall be deducted.
- Determination of market value - There are two possibilities here:
 - The agricultural produce is capable of being sold in the market either in its raw stage or after application of any ordinary process to make it fit to be taken to the market.
 - In such a case, the value calculated at the average price at which it has been so sold during the relevant previous year will be the market value
 - The agricultural produce is not capable of being ordinarily sold in the market in its raw form or after application of any ordinary process. Market value: –
 - The expenses of cultivation;
 - The land revenue or rent paid for the area in which it was grown; and
 - Such amount as the Assessing Officer finds having regard to the circumstances in each case to represent at reasonable profit

Rule 7A – Income From Growing and Manufacturing of Rubber

- 35% profits on sale is taxable as business income under the head “profits and gains from business or profession”, and the balance 65% is agricultural income and is exempt



Example:

- Latex manufactured from the rubber plants grown in India.
- Sold in the market for 60 lacs.
- The cost of growing rubber plants is 20 lacs
- The cost of manufacturing latex is 16 lacs.

Compute his total income.

Solution:

The total income comprises agricultural income and business income.

- Total profits from the sale of latex= 60lacs less 20 lacs less 16 lacs= 24 lacs.
- Agricultural income= 65% of 24 lacs
- Business income= 35% of 24 lacs

Rule 7B – Income from growing and manufacturing of coffee

- Income derived from the sale of coffee grown and cured by the seller in India:
 - 25% profits on sale is taxable as business income under the head “Profits and gains from business or profession”, and the balance 75% is agricultural income and is exempt.
- Income derived from the sale of coffee grown, cured, roasted and grounded by the seller in India, with or without mixing chicory or other flavoring ingredients,
 - 40% x profits on sale is taxable as business income under the head “Profits and gains from business or profession”, and the balance 60% is agricultural income and is exempt.

Rule 8 - Income from Growing and Manufacturing of tea

- 40% taxable as business income under the head “Profits and gains from business or profession”, and

- 60% is agricultural income and is exempt

Income from Farm Building

- The income from such farm building would be agricultural income only if the following conditions are satisfied:
 - The building should be on or in the immediate vicinity of the land; and
 - The receiver of the rent or revenue or the cultivator or the receiver of rent in kind should, by reason of his connection with such land require it as a dwelling house or as a store house.
 - Income from the farm building which is owned and occupied by the receiver of the rent or revenue of any such land or occupied by the cultivator or the receiver of rent in kind, of any land with respect to which, or the produce of which, any process discussed above is carried on, would be agricultural income.
- However, the income arising from the use of such farm building for including letting for residential purpose or for the purpose of business or profession would not be agricultural income.
- In addition to the above conditions any one of the following two conditions should also be satisfied:
 - The land should either be assessed to land revenue in India or be subject to a local rate assessed and collected by the officers of the Government as such or;
 - Where the land is not so assessed to land revenue in India or is not subject to local rate:-
 - It should not be situated in any area as comprised within the jurisdiction of a municipality or a cantonment board and which has a population not less than 10,000 or
 - It should not be situated in any area within such distance, measured aerially, in relation to the range of population as shown hereunder

	Shortest aerial distance from the local limits of a municipality or cantonment board	Population according to the last preceding census of which the relevant figures have been published before the first day of the previous year
(i)	≤ 2 kms	> 10,000
(ii)	>2 kms but ≤ 6 kms	> 1,00,000
(iii)	>6 kms but ≤ 8kms	> 10,00,000



Example:

Agricultural land situated in Mumbai sold for 20 lakhs

Surplus over its cost of acquisition 16 lakhs.

Solution:

- This surplus will not constitute agricultural income exempt under section 10(1) and
- will be taxable under section 45



Example:

- A rural society
- Principal business: the selling on behalf of its member societies, butter made by these societies from cream sold to them by farmers.

- The making of butter was a factory process separated from the farm.

Solution: not an agricultural product



Example:

- The managing agent receives commission at the rate of 20% p.a. on the annual net profits of the company.
- A part of the company's income was agricultural income.

Solution:

Since the remuneration is received under a contract for personal service, does not constitute agricultural income.



Example:

Sale of forest trees of spontaneous growth.

Solution Income from the sale of such forest trees of spontaneous growth does not, therefore, constitute agricultural income

1.4 Examples of Agricultural Income

- Income derived from the sale of seeds.
- Income from growing of flowers and creepers.
- Rent received from land used for grazing of cattle required for agricultural activities.
- Income from growing of bamboo.
- Income from growing trade or commercial products like jute, cotton, etc. is an agro income.
- Plants sold in pots are an agro income provided basic operations are performed.
- Remuneration and interest to partner: Any remuneration (salary, commission, etc.) received by a partner from a firm engaged in agricultural operation is an agro income. Interest on capital received by a partner from a firm, engaged in agricultural operation is an agro income.
- Income arising by sale of trees grown on denuded parts of the forest after replanting and by carrying on subsequent operations is an agro income.
- Compensation received from insurance company for damage caused by hail-storm to the green leaf of the assessee's tea garden is agricultural income.
- Further, no part of such compensation consists of manufacturing income; as such compensation cannot be apportioned under Rule 8 between manufacturing income and agricultural income.
- Any fee derived from land used for grazing of cattle, being used for agricultural operation, is an agro income 8.
- Any income derived from saplings or seedlings grown in a nursery shall be deemed to be agricultural income

1.5 Non-Agricultural Income

- Income from breeding of livestock.
- Income from poultry farming.
- Income from fisheries.
- Income from dairy farming.
- Salary received by an employee from any business (having agricultural income) is non-agro income.

- Dividend received from a company engaged in agricultural operation is non-agro income.
- Income from salt produced by flooding the land with sea-water is non-agro income
- Income from fisheries, poultry farming, dairy farming, butter & cheese making, etc. is non-agro income.
- Breeding & rearing of livestock is non-agro income.
- Interest received by a moneylender in the form of agricultural produce is non-agro income.
- Profit on sale of standing crops after harvest, where such crops were acquired through purchase is non-agro income.
- Royalty income from mines is non-agro income.
- Remuneration to a Director or Managing Director from a company engaged in agricultural business is non-agro income. The provision holds good even when such remuneration is on the basis of certain percentage of net profit.
- Income earned by a cultivator from conversion of sugarcane (raised on own land) to jaggery is non-agro income to the extent to which income is related to such conversion only. This is because sugarcane itself is marketable
- Interest on arrears of rent receivable in respect of agricultural land is non-agro income.
- Income from a land situated outside India is non-agro income
- Annuity received by a person in consideration of transfer of agricultural land, is non-agro income.
- Income on supply of water for agricultural operation is non-agro income. The provision holds well even when such income is received in the form of agro-produce.
- Income from sale of trees and grasses grown spontaneously (without any human effort), is non-agro income
- Profit on transfer of agricultural land: not treated as agricultural income.
- Nexus between agro-activity and agro-income: There must be a close nexus between agro-activity and agro-income.

1.6 Assessee [Section 2(7)]

- “Assessee” means a person by whom any tax or any other sum of money is payable under this Act. In addition, it includes –
- Every person in respect of whom any proceeding under this Act has been taken for the assessment of
- his income; or
- the income of any other person in respect of which he is assessable; or
- the loss sustained by him or by such other person; or
- The amount of refund due to him or to such other person.
- Every person who is deemed to be an assessee under any provision of this Act;
- Every person who is deemed to be an assessee-in-default under any provision of this Act.

1.7 Person [Section 2(31)]

- Seven categories of assesses:
- Individual
- HUF
- AOP/BOI
- Company

Unit 01: Introduction to Basic Concepts of Income Tax Law

- Firm
- Local authority
- Artificial Judicial Person

Individual

- A natural person
- Both males and females
- Minor or a person of unsound mind

HUF

- "Hindu undivided family consists of all males lineally descended from a common ancestor and includes their wives and daughters.
- A Hindu Coparcenary includes those persons who acquire an interest in joint family property by birth.
- Only the coparceners have a right to partition.
- Jain undivided families and Sikh undivided families.

Difference between the two schools of Hindu law

Dayabaga school of Hindu law	Mitakshara school of Hindu law
West Bengal and Assam	Rest of India
Nobody acquires the right, share in the property by birth as long as the head of family is living. Hence, the father and his brothers would be the coparceners of the HUF.	One acquires the right to the family property by his birth.

Company [Section 2(17)]

The expression 'Company' means:

- any Indian company as defined in section 2(26); or
- anybody corporate incorporated by or under the laws of a country outside India, i.e., any foreign company; or

The expression 'Company' means:

- any institution, association or body which is assessable or was assessed as a company for any assessment year under the Indian Income-tax Act, 1922 or for any assessment year commencing on or before 1.4.1970 under the present Act; or
- any institution, association or body, whether incorporated or not and whether Indian or non-Indian, which is declared by a general or special order of the CBDT to be a company for such assessment years as may be specified in the CBDT's order.

Types of Companies

- Domestic company
 - Indian company
 - Company which has made arrangement for declaring and paying dividend within India out of the income chargeable to tax in India.
- Foreign company

Indian Company[Section 2(26)]

- The company should have been formed and registered under the Companies Act, 1956 and
- The registered office or the principal office of the company should be in India.
- The expression 'Indian Company' also includes the following provided their registered or principal office is in India:
 - A corporation established by or under a Central, State or Provincial Act (like Financial Corporation or a State Road Transport Corporation);
 - An institution or association or body which is declared by the Board to be a company under section 2(17)(iv);
 - A company formed and registered under any law relating to companies which was or is in force in any part of India [other than Jammu and Kashmir and Union territories mentioned in sub-clause (v) below];
 - In the case of Jammu and Kashmir, a company formed and registered under any law for the time being in force in Jammu and Kashmir 2(17)(V);
 - In the case of any of the Union territories of Dadra and Nagar Haveli, Daman and Diu, and Pondicherry or State of Goa, a company formed.

Foreign company [Section 2(23A)]

- A company which is not a domestic company

Firm [Section 2(23)]

- As defined under the Partnership Act, 1932
- As defined under the Limited Liability Partnership Act, 2008

Association of Persons (AOP)

- Persons must join for a common purpose or action and their object must be to produce income.

Body of Individuals (BOI)

- Receive the income jointly and who may be assessable in like manner and to the same extent as the beneficiaries individually.
- Income-tax shall not be payable by an assessee in respect of the receipt of share of income by him from BOI and on which the tax has already been paid by such BOI.
- For e.g., mutual trade associations, members clubs, etc.

Difference between AOP and BOI

- In case of a BOI, only individuals can be the members,
- in case of AOP, any person can be its member
- In case of an AOP, :common will for a common intention or purpose,
- in case of BOI, such common will may or may not be present.

Local Authority

Municipal committee, district board, body of port commissioners or other authority legally entitled to or entrusted by the Government with the control or management of a municipal or local fund.

Artificial Juridical Persons

- Not natural persons
- Artificial persons with a juristic personality.
- Example Bar Council, Universities

1.8 Basic Principles for Charging Income Tax [Sec. 4]

- Income of the previous year of a person is charged to tax in the immediately following assessment year.
- The rate of tax is applicable as specified by the Annual Finance Act of that year.
- The tax liability arises at the close of a previous year. The finalization of the amount of tax liability is postponed to the assessment year.

Assessment Year (A.Y.) [Sec. 2(9)]

- Period of 12 months commencing on the 1st day of April every year.
- It is the year (just after the previous year) in which income earned in the previous year is charged to tax.
- E.g., A.Y.2022-23 is a year, which commences on April 1, 2022 and ends on March 31, 2023.
- Income of an assessee earned in the previous year 2021-2022 is assessed in the A.Y. 2022-23.

Previous Year or Uniform Previous Year [Sec. 3]

- The year in which income is earned is known as Previous Year.
- The next year in which income is assessed is known as Assessment Year.
- Previous Year means the financial year immediately preceding the Assessment Year. Income earned in a year is assessed in the next year. The year in which income is earned is known as Previous Year and the next year in which income is assessed is known as Assessment Year. It is mandatory for all assessee to follow financial year (from 1st April to 31st March) as previous year for Income-Tax purpose

Determination of the first previous year of a newly set-up business or profession

- Business or profession being newly set-up:
 - Beginning with the date of setting up of the business & ending on 31st March of that financial year.
- A source of income newly coming into existence.
 - Beginning with the date on which the new source of income comes into existence & ending on 31st March of that financial year.

Exceptions to the general rule that income of a Previous Year is taxed in its Assessment Year

- Income of a non-resident assessee from shipping business (Sec. 172).
- Income of a person who is leaving India either permanently or for a long period (Sec. 174).
- Income of bodies, formed for a short duration (Sec. 174A)
- Income of a person who is likely to transfer property to avoid tax (Sec. 175).
- Income of a discontinued business (Sec. 176).
- In this case, the Assessing Officer has the discretionary power i.e. he may assess the income in the same previous year or may wait till the Assessment year.

Shipping business of non-resident [Section 172]

- 7.5% of the freight paid or payable to the owner or the charterer or to any person on his behalf, whether in India or outside India on account of such carriage is deemed to be his income which is charged to tax in the same year in which it is earned.

Persons leaving India [Section 174]

- Where it appears to the Assessing Officer that any individual may leave India during the current assessment year or shortly after its expiry and he has no present intention of returning to India,
- the total income of such individual for the period from the expiry of the respective previous year up to the probable date of his departure from India is chargeable to tax in that assessment year.

AOP/BOI/Artificial Juridical Person formed for a particular event or purpose [Section 174A]

- If an AOP/BOI etc. is formed or established for a particular event or purpose and the Assessing Officer apprehends that the AOP/BOI is likely to be dissolved in the same year or in the next year,
- He can make assessment of the income up to the date of dissolution as income of the relevant assessment year.

Persons likely to transfer property to avoid tax [Section 175]

- During the current assessment year, if it appears to the Assessing Officer that a person is likely to charge, sell, transfer, dispose of or otherwise part with any of his assets to avoid payment of any liability under this Act,
- The total income of such person for the period from the expiry of the previous year to the date, when the Assessing Officer commences proceedings under this section is chargeable to tax in that assessment year.

Discontinued business [Section 176]

- Where any business or profession is discontinued in any assessment year,
- the income of the period from the expiry of the previous year up to the date of such discontinuance may,
- at the discretion of the Assessing Officer,
- be charged to tax in that assessment year.

1.9 Classification of Income Earned

1. Salary, pension earned is taxable under the head "Salaries".
2. Rental income is taxable under the head "Income from house property".
3. Income derived from carrying on any business or profession is taxable under the head "Profits and gains from business or profession".
4. Profit from sale of a capital asset (like land) is taxable under the head "Capital Gains". The fifth head of income is the residuary head.
5. Income which is chargeable to tax but not taxable under the first four heads will be taxed under the head "Income from other sources".

Notes:

- In the same head of income, there may be various sources of income.
- Exemptions
 - Wholly exempt from income-tax: Agricultural income.
 - Partially exempt from income-tax: House Rent Allowance, Education Allowance.
- Deductions
 - There are deductions and allowances prescribed under each head of income.

Unit 01: Introduction to Basic Concepts of Income Tax Law

- For example, while calculating income from house property, municipal taxes and interest on loan are allowed as deduction.

• Section	• Deduction on	• Allowed Limit (maximum) FY 2021-22
• 80C	<ul style="list-style-type: none"> • Investment in PPF <ul style="list-style-type: none"> - Employee's share of PF contribution - NSCs - Life Insurance Premium payment - Children's Tuition Fee - Principal Repayment of home loan - Investment in Sukanya Samridhi Account - ULIPS - ELSS - Sum paid to purchase deferred annuity - Five year deposit scheme - Senior Citizens savings scheme - Subscription to notified securities/notified deposits scheme 	• Rs. 1,50,000

Clubbing of Income of Spouse, Minor Child etc.

Income arising to certain persons (like spouse, minor child etc.) have to be included in the income of the person who has diverted his income for the purpose of computing tax liability.

Set-off or Carry Forward and Set-off Of Losses

- Set off against different sources of income under the same head of income.
- Inter-head adjustment
- Restrictions on set-off.
- Carry forward

1.10 Computation of Gross Total Income

- The final figures of income or loss under each head of income, after allowing the deductions, allowances and other adjustments, are then aggregated, after giving effect to the provisions for clubbing of income and set-off and carry forward of losses, to arrive at the gross total income.

Summary

- An act to levy, manage, collect, and reclaim income tax in India is the Income Tax Act, 1961. It became effective on April 1st, 1962. Any individual is subject to income tax, along with any applicable surcharges and cess, at the rates outlined in the applicable Central Act for the assessment year. The Income Tax Act provides separate provisions for the taxation of income that has been received in advance as well as income for which the money has not yet been received. When determining his ultimate tax burden at the end of the year, a person must also keep track of the TDS that was deducted. According to the Income Tax Act of 1961, the

preceding year is the financial year that comes right before the assessment year. The prior year for that entity will begin on the date that the business or profession was established, or on the date that the source of income for this new existence began and ended in the specified financial year, whichever is later.

Keywords

Regular receipt: A periodic financial return that accrues or is anticipated to accrue consistently from a specific source is generally referred to as income.

Casual receipt: According to the Income-tax Act of 1961, even some irregular revenues are considered income for tax purposes, such as winnings from lotteries and crossword puzzles.

Net receipt vis-a-vis Gross receipt: Instead of gross receipts, income refers to net receipts. Net receipts are those that remain after deducting the costs associated with generating them. The Income-tax Act of 1961 specifies the expenses that may be subtracted from income when computing income under each head. A fixed percentage of gross receipts is used to determine the income from some eligible businesses and professions on a presumptive basis.

Due basis vis-a-vis receipt basis: Either on a due basis or a receipt basis, income is taxable. The form of accounting that the assessee usually employs should be taken into consideration when calculating income under the heads "Profits and gains of business or profession" and "Income from other sources," which might be either the cash system or the mercantile system. Some receipts, such as income received in the form of interest on compensation or enhanced compensation, are only taxable on a receipt-basis.

Self Assessment

1. Section _____ of the Income Tax Act, 1961 defines income.
 - A. 2(31)
 - B. 2(24)
 - C. 2(9)
 - D. 3

2. A revenue receipt is not which of the following?
 - i. receiving remuneration for the loss of a capital asset
 - ii. Received compensation for a trade asset's loss or damage.
 - iii. gains from the acquisition and sale of shares for his own account by a stock broker.
 - iv. income from renting out properties held by a business to its employees, etc.
 - A. i only
 - B. i and ii both
 - C. i, ii, and iii
 - D. All of the above

3. Person is defined under section _____ of the Income Tax Act, 1961
 - A. 2(31)
 - B. 2(7)
 - C. 2(9)
 - D. 3

4. Company is defined under section _____ of the Income Tax Act, 1961

Unit 01: Introduction to Basic Concepts of Income Tax Law

- A. 2(31)
 - B. 2(7)
 - C. 2(9)
 - D. 2(17)
5. "Assessment year" is defined under section _____ of the Income Tax Act, 1961
- A. 2(31)
 - B. 2(7)
 - C. 2(9)
 - D. 3
6. "Previous year" is defined under section _____ of the Income Tax Act, 1961
- A. 2(31)
 - B. 2(7)
 - C. 2(9)
 - D. 3
7. As per section 2(24), the term income includes all except:
- A. Profits and gains
 - B. Dividend
 - C. Voluntary contributions received by a trust/institution created wholly or partly for charitable or religious purposes or by certain research association or universities and other educational institutions or hospitals and other medical institutions or an electoral trust.
 - D. Gift received for an amount not exceeding Rs. 50,000
8. "Total Income" is defined under section _____ of the Income Tax Act, 1961
- A. 2(31)
 - B. 2(7)
 - C. 2(9)
 - D. 2(45)
9. Which of the following principles is not followed in computation of Total Income?
- A. It is possible to receive income in kind or cash.
 - B. Either on a reception basis or an accrual basis, income is generated.
 - C. Income that has accumulated or arisen from a lawful source and income that has been polluted by illicit activity are distinguished under the income tax laws.
 - D. Under the Act, there is no distinction between temporary and permanent income. According to the Income Tax Act, even temporary income is taxable.
10. Which of the following statement is untrue in regard to Gifts?
- A. Normally, gifts constitute a capital receipt in the hands of the recipient.
 - B. However, certain gifts are brought within the purview of income- tax, under section 56(2)(x).

- C. Gifts of personal nature do not constitute income.
- D. Gifts of personal nature do not constitute income subject to maximum of Rs. 50,000 received in cash.
11. Which of the following statement is untrue in regard to Revenue or Capital receipt?
- A. It is possible to lay down any single test as infallible or any single criterion as decisive, final and universal in application to determine whether a particular receipt is capital or revenue in nature
- B. Therefore, unless the receipt in question constitutes income as distinguished from capital, it cannot be charged to tax.
- C. For this purpose, income should be distinguished from capital which gives rise to income.
- D. However, some capital receipts have been specifically included in the definition of income
12. Which of the following statement is untrue in regard to Previous Year?
- A. Previous year for income tax purposes shall be the calendar year.
- B. Each financial year is both, a previous year as well as an assessment year.
- C. It is the previous year for the income earned during the financial year and assessment year for the income earned during the preceding previous year.
- D. In case of newly set up business or profession or a source of income newly coming into existence, the first previous year will be the period commencing from the date of setting up of business/profession or as the case may be, the date on which the source of income newly comes into existence and ending on the immediately following March, 31.
13. Which of the following definitions is wrong?
- A. An individual is a natural human being i.e. male, female, minor or a person of only sound mind.
- B. Under Income Tax Act, 1961 a Hindu Undivided Family (HUF) is treated as separate entity for the purposes of assessment.
- C. Company includes Domestic company, Foreign company, company in which public are substantially
- D. Firm includes a partnership firm whether registered or not and shall include a Limited Liability Partnership as defined in the Limited Liability Partnership Act, 2008
14. Which of the following statements is wrong in regard to AOP and BOI?
- A. Association of Person means when two or more persons join in for a common purpose or common action to produce income, profits or gains.
- B. Body of Individuals denote the status of persons who are assessable in like manner and to the same extent as the beneficiaries individually
- C. Non-individuals can be the members of BOI
- D. AOP may consist of individuals, HUF, companies, firms, etc. as members
15. The Income of previous year of an assessee is assessed in the previous year itself in following cases except:
- A. Income of persons leaving India either permanently or for long duration

Unit 01: Introduction to Basic Concepts of Income Tax Law

- B. Income of bodies formed for short duration
- C. Income of person trying to transfer his assets with a view to avoid tax
- D. Income of continued business

Answers for Self Assessment

- | | | | | |
|-------|-------|-------|-------|-------|
| 1. B | 2. A | 3. A | 4. D | 5. C |
| 6. D | 7. D | 8. D | 9. C | 10. C |
| 11. A | 12. A | 13. A | 14. C | 15. D |

Review Questions

1. Who can be termed as an "Assessee"?
2. Mention four situations in which the prior year's income was taxable in that year rather than the assessment year.
3. Discuss the steps in computation of total Income [Section 2(45A)]
4. Name five Heads of Income.
5. Define Person u/s 2(31).

**Further Readings**

- https://www.icsi.edu/media/webmodules/16112021_Advance_Tax_Laws.pdf
- Income Tax Law & Practice A.Y 2021-22 by Dr H.C. Mehrotra and Dr. S. P. Goyal. Sahitya Bhawan Publications
- Study Material on Direct Tax Laws and International Taxation by ICAI
- Direct Tax Laws and Practice by Dr. Girish Ahuja & Dr. Ravi Gupta
- <https://www.incometaxindia.gov.in/Charts%20%20Tables/Deductions.htm>

Unit 02: Identification of Residential Status**CONTENTS**

Objectives

Introduction

2.1 Residential Status of an Assessee

2.2 Determination of Residential Status

2.3 Incidence of Tax [Sec. 5]

2.4 Income, Which Do Not Form Part of Total Income

Summary

Keywords

Self Assessment

Answers for Self Assessment

Review Questions

Further Readings

Objectives

After studying this unit, you will be able to:

- Understand the Residential status of an assessee.
- Examine the incidence of tax on the income of a person based on his residential status
- Understand the concept of incomes which do not form part of Total Income

Introduction

The Income Tax Act, 1961, and the Income Tax Rules, 1962, set the rules for income tax collection in India. It is assessed based on total income and Certain terms from the Income Tax Act, such as residential status, assessment year, preceding year, assessee, etc., must be understood in order to calculate the total income. Income tax is imposed on taxable income, and the first steps in determining taxable income are a person's residential status and the extent of their overall income. From a residential perspective, there are two different sorts of taxpayers. India residents and non-India residents. Whether the individual earning the income is a resident or a non-resident, India taxes source-based income. On the other hand, a person's foreign-sourced income is only taxed in India if that person is a resident of India. In order to determine a person's tax liability, it is crucial to establish his or her residence status.

2.1 Residential Status of an Assessee

Sec. 6:

In case of Individual & HUF:

- Ordinarily Resident in India
- Not-ordinarily Resident in India
- Non-Resident

Other:

- Resident in India

- Non-Resident

General Points to be Kept in Mind Residential Status of a Person

- Different for each previous year
- Single Status for each source of income
- Impact of citizenship
- Country Specific

2.2 Determination of Residential Status

Individual [Sec. 6(1)] Resident in India

An individual is said to be a resident in India, if he satisfies any one of the following conditions -

- He is in India in the previous year 182 days or more [Sec. 6(1)(a)]; or
- He is in India 60 days or more during the previous year and for 365 or more days during 4 previous years immediately preceding the relevant previous year [Sec. 6(1)(c)]

Individual [Sec. 6(1)] Non- Resident in India

An assessed who is not satisfying sec. 6(1) shall be treated as a non-resident in India for the relevant previous year.

Exceptions to the Rule

A. In the following cases, condition (ii) of sec. 6(1) [i.e. sec. 6(1)(c)] is irrelevant:

- An Indian citizen who leaves India during the previous year for employment purpose.
- An Indian citizen who leaves India during the previous year as a member of crew of an Indian ship.

B. In case of an Indian citizen or a person of Indian origin# comes on a visit to India during the previous year, modified condition (ii) of sec. 6(1) is applicable:

- His total income, other than the income from foreign sources exceeds 15 lakhs during the previous year

He is in India for a period of 120 days or more (but less than 182 days) during the previous year and for 365 or more days during 4 previous years immediately preceding the relevant previous year

- His total income, other than the income from foreign sources, does not exceed 15 lakhs during the previous year

He is in India for a period of 182 days or more during the previous year

C. An individual shall be deemed to be resident in India if the following conditions are satisfied

- He is a citizen of India
- His total income, other than the income from foreign sources, exceeds 15 lakhs during the previous year;
- He is not satisfying any of the basic conditions given u/s 6(1) [i.e., 182 days or 60 days + 365 days];
- He is not liable to tax in any other country or territory because of his domicile or residence or any other criteria of similar nature. [Sec. 6(1A)]

Additional Conditions to Test Whether Resident Individual is 'Ordinarily Resident or Not' [Sec. 6(6)]

A resident individual further categorised as -

- Resident and ordinarily resident in India
- Resident but not ordinarily resident in India

Unit 02: Identification of Residential Status**Resident and Ordinarily Resident**

If a resident individual satisfies the following two additional conditions, he will be treated as resident & ordinarily resident in India –

- a. He has been resident in India [as per sec. 6(1)] in at least 2 out of 10 previous years immediately preceding the relevant previous year;
- b. He has resided in India for 730 days or more during 7 previous years immediately preceding the relevant previous year

Resident but Not Ordinarily Resident

If a resident individual does not satisfy both additional conditions as given u/s 6(6), he is “Resident but not ordinarily resident in India”.

Exceptions

A. An individual shall be deemed to be resident but not ordinarily resident in India, if following conditions are satisfied:

- a. He is a citizen of India
- b. His total income, other than the income from foreign sources, exceeds ₹ 15 lakhs during the previous year; and
- c. He is not liable to tax in any other country or territory because of his domicile or residence or any other criteria of similar nature.
- d. He is deemed to be resident in India u/s 6(1A).

B. An individual shall be deemed to be resident but not ordinarily resident in India if the following conditions are satisfied:

- a. He is an Indian citizen or a person of Indian origin.
- b. He comes on a visit to India during the previous year
- c. His total income, other than the income from foreign sources, exceeds ₹ 15 lakhs during the previous year
- d. He is in India for 120 days or more (but less than 182 days) during the previous year and for 365 or more days during 4 previous years immediately preceding the relevant previous year

Hindu Undivided Family (HUF) [Sec. 6(2)]

An HUF can be either a

resident (‘Ordinarily resident’ and ‘Not ordinarily resident’)

or

non-resident

Resident HUF

When the control & management of affairs of HUF is wholly or partly situated in India during the relevant previous year.

Non-Resident HUF

An HUF is non-resident in India if the control & management of its affairs is wholly situated outside India.

Ordinarily Resident HUF

- If the ‘Karta’ or manager of a resident HUF satisfies both additional conditions given u/s 6(6), HUF is said to be an ordinarily resident.
- If the ‘Karta’ or manager of a resident HUF does not satisfy both additional conditions given u/s 6(6), HUF is said to be a not-ordinarily resident

Company [Sec. 6(3)]

Income Tax Law and Practice

- Non-Resident Company: If place of effective management in that year is not in India.
- Resident Company: An Indian company is always a resident in India.

Non-Resident Company: If the place of effective management in that year is not in India the said company is non-resident in India for the relevant previous year.

- Tax point: In the case of a company, there is no sub-division like 'Ordinarily resident' or 'Not ordinarily resident.'

Firm or an Association of Persons (AOP) or Body of Individuals (BOI) [Sec. 6(4)]

- Resident if control & management of its affairs are wholly or partly situated in India during the relevant previous year.
- Non-resident: If control & management of its affairs are situated wholly outside India.
- Resident: A firm or an AOP or BOI is said to be a resident in India if control & management of its affairs are wholly or partly situated in India during the relevant previous year. Control & management is vested in hands of partners in the case of a firm and the principal officer in the case of an AOP/BOI.
- Non-resident: If control & management of its affairs are situated wholly outside India, then it is a non-resident in India. Tax point: In the case of firm or BOI or AOP, there is no subdivision like 'Ordinarily resident' or 'Not ordinarily resident'

Any Other Person

- Resident: if the control & management of its affairs is situated wholly or partly in India.
- Non-Resident: If control & management of affairs of the assessee are situated wholly outside India.

2.3 Incidence of Tax [Sec. 5]

The incidence of tax on any person depends

- the residential status of the assessee;

the place of accrual or receipt of income, whether actual or deemed; and

- the point of time at which the income had accrued to or was received by or on behalf of the assessee.

Nature of Income	Tax incidence in the case of		
	Resident & ordinarily resident	Resident but not ordinarily resident	Non resident
Income accrued or deemed to be accrued and received or deemed to be received in India	Taxable	Taxable	Taxable
Income accrued outside India but received or deemed to be received in India	Taxable	Taxable	Taxable
Income accrued or deemed to be accrued in India but received outside India	Taxable	Taxable	Taxable

Unit 02: Identification of Residential Status

Income accrued and received outside India from a business controlled in or profession set-up in India.	Taxable	Taxable	Not Taxable
Income accrued and received outside India from a business controlled or profession set-up outside India.	Taxable	Not Taxable	Not Taxable
Income accrued and received outside India in the previous year (it makes no difference if the same is later remitted to India).	Taxable	Not Taxable	Not Taxable
Income accrued and received outside India in any year preceding the previous year and later on remitted to India in current financial year.	Not Taxable	Not Taxable	Not Taxable

Resident and Ordinarily Resident

- Income received or deemed to be received in India during the previous year;
- Income which accrues or arises or is deemed to accrue or arise in India during the previous year; and
- Income that accrues or arises outside India even if it is not received or brought into India during the previous year.

Resident but not Ordinarily Resident

- Income received or deemed to be received in India during the previous year;
- Income which accrues or arises or is deemed to accrue or arise in India during the previous year; and
- Income derived from a business controlled in or profession set up in India, even though it accrues or arises outside India.

Non-resident

- Income received or deemed to be received in India in the previous year; and
- Income that accrues or arises or is deemed to accrue or arise in India during the previous year.

Income Received in India

- Taxable in all cases

Income Deemed to Be Received in India

- The annual accretion in the previous year to the balance at the credit of an employee participating in a recognised provident fund, to the extent provided in Rule 6 of part A of the IV schedule i.e.-
 - Employer's contribution to the recognised provident fund in excess of 12% of salary.
 - Interest credited on the above balance by a rate exceeding 9.5% [Sec. 7(i)]
- The transferred balance in recognised provident fund, to the extent liable to income tax [Sec. 7(ii)]
- The contribution made, by the employer in the previous year, to the account of an employee under a pension scheme notified u/s 80CCD [Sec. 7(iii)]
- Tax Deducted at source [Sec. 198]

Income Tax Law and Practice

- e. Deemed profit.
- f. Income from undisclosed sources

Income Deemed To Accrue Or Arise In India [Sec. 9]

- Income from connection in India
- Salary earned in India
- Salary from Govt. by an Indian citizen for services rendered outside India
- Income from dividend paid by an Indian company

Income from interest payable by specified person

- Income from royalty
- Income from technical services
- Deemed receipt of gift by non-resident

Meaning of Accrual

- Accrue refers to the right to receive income.
- On Government securities,
 - ✓ interest payable on specified dates arise during the period of holding,
 - ✓ become due for payment on the specified date

Income from connection in India [Sec. 9(1)(i)]

All income accruing or arising, whether directly or indirectly,

- a. through or from any business connection in India; or
- b. through or from any property / asset or source of income in India; or
- c. through the transfer of a capital asset situated in India.

Income from a business connection in India

- Taxable in hands of all assessee.

Meaning of Business Connection:

The business connection shall include any business activity carried out through a person who, acting on behalf of the non-resident:

- a. has and habitually exercises in India, an authority to conclude contracts on behalf of the non-resident or habitually concludes contracts or habitually plays the principal role leading to conclusion of contracts by that non-resident and the contracts are—
[Explanation 4]
 1. In the name of the non-resident; or
 2. For the transfer of the ownership of, or for the granting of the right to use, property owned by that non-resident or that non-resident has the right to use; or
 3. For the provision of services by the non-resident; or
- b. has no such authority, but he maintains in India habitually a stock of goods or merchandise from which he regularly delivers goods or merchandise on behalf of the non-resident; or
- c. habitually secures orders in India mainly for the non-resident.

Further, there may be situations when the person acting on behalf of the non-resident secures order for other non-residents.

Income from connection in India [Sec. 9(1)(i)]

All income accruing or arising, whether directly or indirectly,:

- a. Through or from any business connection in India; or

Unit 02: Identification of Residential Status

- b. Through or from any property / asset (whether tangible / intangible, movable / immovable;) or source of income in India; or
- c. Through the transfer of a capital asset situated in India.

Through the transfer of a capital asset situated in India.

Irrespective of the fact whether

1. Movable/immovable/tangible/ intangible;
2. the place of registration of the document of transfer etc., is in India /outside; and
3. the place of payment of the consideration for the transfer is within India /outside.

Exceptions

1. Business activity through a broker
2. Business activity confined to purchase of goods:
3. Business activity of a news agency confined to collection of news, etc.:
4. Business of mining of diamonds:
5. Business activity confined to shooting:

Notes:

In the case of a business of which all operations are not carried out in India, the income of the business deemed to accrue or arise in India shall be only such part of the income as is reasonably attributable to the operations carried out in India. [Explanation 1(a)]

An asset or a capital asset being any share or interest in a company or entity registered or incorporated outside India shall be deemed to be situated in India, if the share or interest derives, directly or indirectly, its value substantially from the assets located in India. [Explanation 5].

Significant economic presence

- transaction in respect of any goods, services, or property carried out by a non-resident with any person in India including the provision of download of data or software in India, if the aggregate of payments arising from such transaction or transactions during the previous year exceeds such amount as may be prescribed

Significant economic presence: Prescribed amounts

- a. in respect of any goods, services or property carried out by a non-resident with any person in India including provision of download of data or software in India
 - Aggregate of payments arising from such transaction or transactions during the previous year should exceed 2 crores.
- b. systematic and continuous soliciting of business activities or engaging in interaction with users in India
 - The number of users should be atleast 3 lakhs.

The transactions or activities shall constitute significant economic presence in India

Whether or not:

- i. the agreement for such transactions or activities is entered in India; or
- ii. the non-resident has a residence or place of business in India; or
- iii. the non-resident renders services in India:

income as is attributable to the transactions or activities

- Only so much of income as is attributable to the transactions or activities referred above shall be deemed to accrue or arise in India.
- The income attributable to the operations carried out in India shall include income from:

Income Tax Law and Practice

- such advertisement which targets a customer who resides in India or a customer who accesses the advertisement through an internet protocol address located in India;
- sale of data collected from a person who resides in India or from a person who uses an internet protocol address located in India; and
- sale of goods or services using data collected from a person who resides in India or from a person who uses an internet protocol address located in India.
- In the case of an eligible investment fund, the fund management activity carried out through an eligible fund manager acting on behalf of such fund shall not constitute a business connection in India of the said fund [Sec. 9A]

Salaries earned in India [Sec. 9(1)(ii)]

Salary payable for -

- Services rendered in India; and
- The rest period or leave period which is preceded and succeeded by the period during which services were rendered in India and forms part of the service contract of employment.

Salary payable by the Government to Indian citizen for services rendered outside India [Sec. 9(1)(iii)]

Any salary -

- payable by the Government of India;
- to a citizen of India;
- for services rendered outside India;

Income from dividend [Sec. 9(1)(iv)]

- Any dividend paid by an Indian company outside India
- is deemed to accrue or arise in India.

Income from Interest [Sec. 9(1)(v)]

- Interest payable by the Government.
- Interest payable by A resident person
 - Provided money borrowed is not used for the purpose of business or profession carried on by such person outside India; or
 - Provided money borrowed is not used for the purpose of earning any income from any source outside India.
- Interest payable by A non-resident person:
 - Provided money borrowed is used for business or profession carried on by such person in India.

Income from royalty [Sec. 9(1)(vi)]

- Royalty payable by the Government.
- Royalty payable by a resident person provided:
 - The right, property, information, or services are not utilized for the purpose of
 - business or profession carried on by such person outside India; or
 - earning any income from any source outside India
- Royalty payable by a non-resident person provided:
 - The right, property, information or services must be utilised for the purpose of
 - business or profession carried on by such person in India; or
 - earning any income from any source in India

Notes on Royalty

Unit 02: Identification of Residential Status

- Lumpsum royalty not deemed to accrue arise in India.
- in respect of computer software supplied by a non-resident manufacturer along with computer hardware under any scheme approved by the Government under the Policy on Compute Software Export, Software Development and Training, 1986
- The definition of 'royalty' covers both industrial royalties as well as copyright royalties.

Income from technical services [Sec. 9(1)(vii)]

- Fee for technical services payable by the Government.
- Fee for technical services payable by A resident person provided:
 - Such services must not be utilised in –
 - business or profession carried on by such person outside India; or
 - earning any income from any source outside India
- Fee for technical services payable by A non-resident person:
- Such services must be utilized in –
 - business or profession carried on by such person in India; or
 - earning any income from any source in India.

Deemed Receipts of Gift [Sec. 9(1)(viii)]

When

- a non-resident or a foreign company receives any sum of money referred to in sec. 56(2)(x)³
- such receipt is from a resident person
- such money is received outside India
- such money is received on or after 05-07-2019

Then such receipt is treated as income deemed to accrue or arise in India.

2.4 Income, Which Do Not Form Part of Total Income

- ***Agricultural Income [Sec. 10(1)]***
- ***Member's Share in Income of HUF [Sec. 10(2)]***
- ***Share of Profit from a Firm [Sec. 10(2A)]***
- ***Interest Income of Non-resident [Sec. 10(4)/(4B)]***
- Interest on specified securities or bonds, including premium on redemption of such bonds is exempted in the hands of a non-resident [Sec. 10(4)(i)]
- Interest on Non-Resident (External) Account in any bank in India to a person who is a resident outside India as per as defined in sec. 2(w) of the Foreign Exchange Management Act, 1999 or is a person who has been permitted by the Reserve Bank of India to maintain the aforesaid Account
- Interest on notified savings certificates issued before 1-6-2002 by the Central Government to a non-resident, being a citizen of India or a person of Indian origin [Sec. 10(4B)]

Interest on Rupee Denominated Bond [Sec. 10(4C)]

- Interest payable to a non-resident, not being a company, or to a foreign company, is exempt if following conditions are satisfied:
 - a. Interest is payable by any Indian company or business trust.
 - b. Such interest is payable in respect of monies borrowed from a source outside India by way of issue of rupee denominated bond, as referred to in sec. 194LC(2)(ia).

- c. Such bond has been issued during 17-09-2018 and 31-03-2019.

Income received by specified fund [Sec. 10(4D)] Amended

- Any income accrued or arisen to, or received by a specified fund as a result of transfer of capital asset referred to in sec. 47(viiab), on a recognized stock exchange located in any International Financial Services Centre; and
- Where the consideration for such transaction is paid or payable in convertible foreign exchange or as a result of transfer of securities (other than shares in a company resident in India) or any income from securities issued by a non-resident (not being a permanent establishment of a non-resident in India); and
- Where such income otherwise does not accrue or arise in India or any income from a securitization trust which is chargeable under the head "Profits and gains of business or profession", -
- To the extent such income accrued or arisen to, or is received, is attributable to units held by non-resident (not being the permanent establishment of a non-resident in India) or is attributable to the investment division of offshore banking unit, as the case may be, computed in the prescribed manner.

Income of IFSC [Sec. 10(4E)/4(F)] New

- Any income accrued or arisen to, or received by a non-resident as a result of transfer of non-deliverable forward contracts entered into with an offshore banking unit of an International Financial Services Centre as referred to in sec. 80LA(1A), which fulfils such conditions as may be prescribed;
- Any income of a non-resident by way of royalty or interest, on account of lease of an aircraft in a previous year, paid by a unit of an International Financial Services Centre, if the unit has commenced its operations on or before 31-03-2024.
- Any income accrued or arisen to, or received by a non-resident as a result of transfer of non-deliverable forward contracts entered into with an offshore banking unit of an International Financial Services Centre as referred to in sec. 80LA(1A), which fulfils such conditions as may be prescribed;
- Any income of a non-resident by way of royalty or interest, on account of lease of an aircraft in a previous year, paid by a unit of an International Financial Services Centre, if the unit has commenced its operations on or before 31-03-2024.
- "Aircraft" means an aircraft or a helicopter, or an engine of an aircraft or a helicopter, or any part there.

Remuneration to Person who is not a Citizen of India in certain cases [Sec. 10(6)]

- Remuneration received by him as an official of an embassy, high commission, legation, commission, consulate, or the trade representation of a foreign state or as a staff of any of these officials provided corresponding Indian officials in that foreign country enjoy similar exemptions in their country - Sec. 10(6)(ii).
- Remuneration received as an employee of a foreign enterprise for services rendered by him during his stay in India provided -
 - a. the foreign enterprise is not engaged in any business or profession in India;
 - b. his stay in India does not exceed 90 days in aggregate; and
 - c. such remuneration is not liable to be deducted from the income of the employer under this Act - Sec. 10(6)(vi)

Unit 02: Identification of Residential Status

- Remuneration for services rendered in connection with his employment on a foreign ship provided his total stay in India does not exceed 90 days in the previous year - Sec. 10(6)(viii)
- Remuneration received as an employee of the Government of a foreign State during his stay in India in connection with his training in any undertaking owned by Government, Government company, subsidiary of a Government company, corporation established by any Central, State or Provincial Act and any society wholly financed by the Central or State Government – Sec. 10(6)(xi)

Income, Which Do Not Form Part of Total Income

- Tax paid by Government on Royalty or Fees for Technical Service [Sec. 10(6A)]
- Tax paid by Government on Income of a Non-resident or a Foreign Company [Sec. 10(6B)]
- Tax paid on Income from Leasing of Aircraft [Sec. 10(6BB)]
 - Tax paid by an Indian company on income arising from leasing of aircraft, etc.
 - to the Government of a foreign state or foreign enterprise under an approved agreement entered into with such Indian company engaged in the business of operation of aircraft,
 - provided such agreement was entered into between 1-4-1997 and 31-3-1999 or after 31-3-2007.
- Fees for Technical Services in Project connected with Security of India [Sec. 10(6C)]
- Income from service provided to National Technical Research Organization [Sec. 10(6D)]
- Allowance or Perquisite paid Outside India [Sec. 10(7)]
- Remuneration received for Co-operative Technical Assistance Programmes with an Agreement entered into by the Central Government in certain cases [Sec. 10(8)]
- Remuneration received by Non-resident Consultant or Employee or Family Member of such Consultant [Sec. 10(8A), (8B) & (9)]
- [Sec. 10(7)] Any allowance or perquisite paid outside India by the Government to a citizen of India for rendering services outside India.
- [Sec. 10(6D)] Any income arising to a non-resident or to a foreign company, by way of royalty from, or fees for technical services rendered in or outside India to, the National Technical Research Organization Allowance or Perquisite paid Outside India
- Compensation under Bhopal Gas Leak Disaster Act, 1985 [Sec. 10(10BB)]
- Compensation for any Disaster [Sec. 10(10BC)]
- Any sum received under a life insurance policy including bonus on such policy is wholly exempt from tax. However, exemption is not available on
 - any sum received u/s 80DD(3) or u/s 80DDA(3); or
 - any sum received under a Keyman insurance policy; or
 - any sum received under an insurance policy issued on or after 1-4-2012 in respect of which the premium payable for any of the years during the term of the policy exceeds 10% of the actual capital sum assured.
 - Where any unit linked insurance policy (ULIP), is issued on or after 01-02-2021 and the premium payable for any of the previous year during the term of such policy exceeds Rs.2,50,000
 - Where the premium is payable, by a person, for more than one ULIP, issued on or after 01-02-2021, the exemption shall apply only with respect to those ULIP, where the aggregate amount of premium does not exceed the aforesaid limit in any of the previous year during the term of any of those policies

Payment from Statutory or Public Provident Fund [Sec. 10(11)] Amended

- Exceptions
 - Interest accrued during the previous year in the account of an employee maintained by the fund shall not be exempted to the extent it relates to the following amount:
 - Where employer is giving contribution: Interest on employee's contribution (made on or after 01-04-2021) in excess of ₹ 2,50,000 per year not exempted
 - Where employer is not giving contribution: Interest on employee's contribution (made on or after 01-04-2021) in excess of ₹ 5,00,000 per year
- Payment from Sukanya Samriddhi Account [Sec. 10(11A)]
- Payment from Recognised Provident Fund [Sec. 10(12)] Amended
 - Exceptions
- Interest accrued during the previous year in the account of an employee maintained by the fund shall not be exempted to the extent it relates to the following amount:
 - Where employer is giving contribution : Interest on employee's contribution (made on or after 01-04-2021) in excess of ₹ 2,50,000 per year not exempted
 - Where employer is not giving contribution: Interest on employee's contribution (made on or after 01-04-2021) in excess of ₹ 5,00,000 per year not exempted
- Payment from National Pension Trust [Sec. 10(12A) & 10(12B)]
 - on closure of his account or on his opting out of the pension scheme referred to in sec. 80CCD, to the extent it does not exceed 60% of the total amount payable to him at the time of such closure or his opting out of the scheme [Sec. 10(12A)].
 - partial withdrawal made out of his account in accordance with the terms and conditions, specified under the Pension Fund Regulatory and Development Authority Act, 2013, to the extent it does not exceed 25% of the amount of contributions made by him [Sec. 10(12B)]
- Payment from Approved Superannuation Fund [Sec. 10(13)]
 - Any payment from an approved superannuation fund made –
 - on the death of a beneficiary; or
 - to an employee in lieu of or in commutation of an annuity on his retirement at or after a specified age or on his becoming incapacitated prior to such retirement; or
 - by way of refund of contributions on the death of a beneficiary; or
 - by way of refund of contributions to an employee on his leaving the service (otherwise than by retirement at or after a specified age or on his becoming incapacitated prior to such retirement) to the extent to which such payment does not exceed the contributions made prior to 1-4-1962 and any interest thereon.
 - by way of transfer to the account of the employee under a pension scheme referred to in sec. 80CCD and notified by the Central Government
- Interest on Securities [Sec. 10(15)]
 - Interest, premium on redemption or other payment on notified securities, bonds or certificates
 - Interest in the hands of an individual and Hindu undivided family on Specified Capital Investment Bonds or Specified Relief Bonds
 - Interest on specified bonds to non-resident or his nominees if such bonds are purchased by a non-resident Indian in foreign exchange; and
 - The interest and principal received in respect of such bonds, whether on their maturity or otherwise, is not allowable to be taken out of India. Interest on securities held by the Issue Department of the Central Bank of Ceylon;

Unit 02: Identification of Residential Status

- Interest payable to any bank incorporated in a country outside India and authorised to perform central banking functions in that country on any deposits made by it, with the approval of the RBI, with any scheduled bank;
- Interest payable on a loan advanced by the Nordic Investment Bank for an approved project;
- Interest payable to the European Investment Bank for financial co-operation agreement;
- Interest payable by a Government, local authority, certain industrial undertakings or financial institution on money borrowed before 1/6/2001
- Interest on securities held by the Welfare Commissioner, Bhopal Gas Victims or deposits for the benefit of the victims of the Bhopal gas leak disaster.
- Interest on Gold Deposit Bonds issued under the Gold Deposit Scheme, 1999 or deposit certificates issued under the Gold Monetisation Scheme, 2015
- Interest on specified bonds issued by a local authority or by a State Pooled Finance Entity.
- Interest received by a non-resident or a person who is not ordinarily resident, in India on a deposit made on or after 1-4-2005 in an offshore banking unit referred in the Special Economic Zones Act, 2005
- Interest payable to a non-resident by a unit located in an International Financial Services Centre in respect of monies borrowed by it on or after 01-09-2019

Income from Leasing of Aircraft [Sec. 10(15A)]

- Any payment made, by an Indian company engaged in the business of operation of aircraft, to acquire an aircraft or an aircraft engine (other than a payment for providing spares, facilities or services in connection with the operation of leased aircraft) on lease from the foreign Government or a foreign enterprise under an approved agreement. The agreement must not be entered into –
 - between 1-4-1997 to 31-3-1999; and
 - on or after 1-4-2007

SCHOLARSHIP [SEC. 10(16)]

To meet the cost of education

DAILY ALLOWANCE, ETC. TO MP AND MLA [SEC. 10(17)]

- Any income by way of
 - Daily allowance received by any person by reason of his membership of Parliament or of any State Legislature or of any Committee thereof;

Any allowance received by any person by reason of his membership of Parliament;

Constituency Allowance received by any person by reason of his membership of State legislature;

AWARDS AND REWARDS [SEC. 10(17A)]

Any payment made, whether in cash or in kind:

- in pursuance of any award instituted in the public interest by the Central Government or any State Government or by any other approved body; or
- as a reward by the Central Government or any State Government for approved purposes.

Pension to receiver of Gallantry Awards [Sec. 10(18)]

Any income by way of

- pension received by an individual who has been in the service of the Central or State Government and has been awarded “Param Vir Chakra” or “Maha Vir Chakra” or “Vir Chakra” or such other notified gallantry award³; or

Income Tax Law and Practice

- family pension received by any member of the family of such individual.

Family Pension to Widow or Children of Armed Force [Sec. 10(19)]

- Family pension received by the widow or children or nominated heirs, of a member of the armed forces (including para-military forces) of the Union, where the death of such member has occurred in the course of operational duties, in such circumstances and subject to such conditions, as may be prescribed.

PALACE OF EX-RULER [SEC. 10(19A)]

- The annual value in respect of any one palace, which is in the occupation of an ex-ruler.

INCOME OF LOCAL AUTHORITY [SEC. 10(20)]

- Income chargeable under the head Income from House Property, Capital Gains or Income from other Sources
- Income from the supply of commodities (other than water or electricity) or services, within its own jurisdiction
- Income from the supply of water services or electricity within or outside its jurisdiction

INCOME OF SCIENTIFIC RESEARCH ASSOCIATION [SEC. 10(21)]

- Any income of a scientific research association [being approved for the purpose of Sec. 35(1)(ii)] or
- research association which has its object, undertaking research in social science or statistical research [being approved and notified for the purpose of Sec. 35(1)(iii)], is exempt provided such association –
 - applies its income, or accumulates it for application, wholly and exclusively to the objects for which it is established; and
 - invest or deposit its funds in specified investments

Income of News Agency [SEC. 10(22B)]

set up in India solely for collection and distribution of news shall be exempt provided:

- a. The news agency applies its income or accumulates it for application solely for collection and distribution of news; and
- b. It does not distribute its income in any manner to its members.

INCOME OF PROFESSIONAL INSTITUTIONS [SEC. 10(23A)]

provided

- Such association or institution is established in India having as its object the control, supervision, regulation or encouragement of the profession of law, medicine, accountancy, engineering or architecture or other specified profession;
- Such association or institution applies its income, or accumulates it for application, solely to the objects for which it is established; and
- The association or institution is approved by the Central Government.

INCOME, WHICH DO NOT FORM PART OF TOTAL INCOME

- Income of Regimental Fund [Sec. 10(23AA)]
- Income of trust for Development of Khadi and Village Industries [Sec. 10(23B)]
- Income of Khadi and Village Industries Boards [Sec. 10(23BB)]
- Income of body formed for Administration of Public Religious or Charitable Trusts [Sec. 10(23BBA)]
- Income of Regimental Fund [Sec. 10(23AA)]

Unit 02: Identification of Residential Status

- Income of trust for Development of Khadi and Village Industries [Sec. 10(23B)]
- Income of Khadi and Village Industries Boards [Sec. 10(23BB)]
- Income of body formed for Administration of Public Religious or Charitable Trusts [Sec. 10(23BBA)]
- Income of European Economic Community [Sec. 10(23BBB)]
- Income of SAARC Fund [Sec. 10(23BBC)]
- Income of ASOSAI-SECRETARIAT [Sec. 10(23BBD)] Income of Insurance Regulatory Authority [Sec. 10(23BBE)]
- Income of the Central Electricity Regulatory Commission [Sec. 10(23BBG)]
- Income of body formed for Administration of Public Religious or Charitable Trusts [Sec. 10(23BBA)]
- Income of the Prasar Bharati (Broadcasting Corporation of India) [Sec. 10(23BBH)]

INCOME OF CERTAIN FUNDS [SEC. 10(23C)] AMENDED

- The Prime Minister's National Relief Fund or the Prime Minister's Citizen Assistance and Relief in Emergency Situations Fund (PM CARES FUND); [sec. 10(23C)(i)]
- The Prime Minister's Fund (Promotion of Folk Art); [sec. 10(23C)(ii)]
- The Prime Minister's Aid to Students Fund; [sec. 10(23C)(iii)]
- The National Foundation for Communal Harmony; [sec. 10(23C)(iiia)]
- The Swachh Bharat Kosh; [sec. 10(23C)(iiiiaa)]
- The Clean Ganga Fund; [sec. 10(23C)(iiiiaaa)]
- The Chief Minister's Relief Fund or the Lieutenant Governor's Relief Fund; [sec. 10(23C)(iiiiaaaa)]
- Any other charitable fund or institution notified by the prescribed authority (subject to condition) [sec. 10(23C) (iv)]
- Any trust or institution wholly for public religious purposes or wholly for public religious and charitable purposes notified by the prescribed authority (subject to conditions) [sec. 10(23C)(v)]
- Any university or other education institutions, (wholly or substantially financed by Government or having annual receipt of prescribed limit upto 5 crores) existing solely for education purposes and not for profit. [sec.10(23C)(iiiic), (iiiid) (vi)]
- Any hospital or other institution (wholly or substantially financed by Government or having annual receipt up to 5 crores) for treatment of person suffering from illness or mental defectiveness or during convalescence or requiring medical attention or rehabilitation, existing solely for philanthropic purposes and not for profit. [sec.10(23C)(iiiic), (iiiie) and (via)]
- Income of Securitisation Trust [Sec. 10(23DA)]
- Income of Mutual Fund [Sec. 10(23D)]
- Income of Investor Protection Fund [Sec. 10(23EA)]
- Income of Credit Guarantee Fund Trust for Small Industries [Sec. 10(23EB)]
- Income of Investor Protection Fund set up by Commodity Exchange [Sec. 10(23EC)]
- Income of Investor Protection Fund of Depositories [Sec. 10(23ED)]
- Income of Core Settlement Guarantee Fund [Sec. 10(23EE)]
- Income of Ventures Capital Fund or Venture Capital Company [Sec 10(23FB)]
- Non-business income of Investment Fund [Sec. 10(23FBA)]

Summary

Without knowing a person's residency status in India the previous year, it is impossible to calculate their total income. Only if the person is an Indian resident is income generated and received outside of India taxable in India. It indicates that resident assesseees have a higher scope or tax incidence, and that one can plan his residential status as a fundamental instrument of tax planning in his arsenal to lessen his tax burden. The tests to be used to assess each tax payer's residence status for income-tax purposes are outlined in Section 6 of the Income-tax Act.

Keywords

“Place of effective management” means a place where key management and commercial decisions that are necessary for the conduct of the business of an entity as a whole, are in substance made.’

Passive income” The total of a company's "passive income" is the money it makes through its transactions, where both the selling and acquisition of items are made by or to its affiliated businesses; and earnings from rent, royalties, dividends, capital gains, or interest;

Senior Management: When referring to a company, "Senior Management" refers to the person or people who are typically in charge of creating and formulating important strategies and policies for the business as well as ensuring or supervising the execution and implementation of those strategies on a regular and ongoing basis.

Self Assessment

1. In case of Payment from Recognized Provident Fund [Sec. 10(12)], where employer is giving contribution, Interest on employee’s contribution (made on or after 01-04-2021) in excess of Rs..... per year not exempted
 - A. 2,50,000
 - B. 3,50,000
 - C. 4,50,000
 - D. 5,00,000

2. In case of Payment from Recognised Provident Fund [Sec. 10(12)], where employer is not giving contribution: Interest on employee’s contribution (made on or after 01-04-2021) in excess of Rs..... per year not exempted
 - A. 2,50,000
 - B. 3,50,000
 - C. 4,50,000
 - D. 5,00,000

3. In case of Payment from National Pension Trust [Sec. 10(12A) & 10(12B)], on closure of his account or on his opting out of the pension scheme referred to in sec. 80CCD, to the extent it does not exceed% of the total amount payable to him at the time of such closure or his opting out of the scheme [Sec. 10(12A)].
 - A. 50
 - B. 60
 - C. 70
 - D. 80

4. In case of Payment from National Pension Trust [Sec. 10(12A) & 10(12B)], partial withdrawal made out of his account in accordance with the terms and conditions, specified under the Pension Fund Regulatory and Development Authority Act, 2013, to

Unit 02: Identification of Residential Status

- the extent it does not exceed% of the amount of contributions made by him [Sec. 10(12B)]
- A. 25
 - B. 30
 - C. 35
 - D. 40
5. In case of annual accretion in the previous year to the balance at the credit of an employee participating in a recognized provident fund, to the extent provided in Rule 6 of part A of the IV schedule Employer's contribution to the recognised provident fund in excess of% of salary is the Income Deemed To Be Received In India.
- A. 10
 - B. 12
 - C. 13
 - D. 14
6. In case of annual accretion in the previous year to the balance at the credit of an employee participating in a recognized provident fund, to the extent provided in Rule 6 of part A of the IV schedule i.e. Interest credited on the above balance by a rate exceeding % [Sec. 7(i)] is the Income Deemed To Be Received In India.
- A. 9.5
 - B. 12
 - C. 13
 - D. 14
7. Income accrued and received outside India from a business controlled or profession set-up outside India is taxable in following case:
- A. Resident & ordinarily resident
 - B. Resident but not ordinarily resident
 - C. Non resident
 - D. Taxable in all cases
8. Income accrued and received outside India from a business controlled in or profession set-up in India is not taxable in case of:
- A. Resident & ordinarily resident
 - B. Resident but not ordinarily resident
 - C. Non resident
 - D. Taxable in all cases
9. Income accrued and received outside India in any year preceding the previous year and later on remitted to India in current financial year is taxable in following case:
- A. Resident & ordinarily resident
 - B. Resident but not ordinarily resident
 - C. Non resident
 - D. Not Taxable in all cases

10. Income accrued or deemed to be accrued in India but received outside India is taxable in not taxable in:
- A. Resident & ordinarily resident
 - B. Resident but not ordinarily resident
 - C. Non resident
 - D. Taxable in all cases
11. Income accrued outside India but received or deemed to be received in India in not taxable in:
- A. Resident & ordinarily resident
 - B. Resident but not ordinarily resident
 - C. Non resident
 - D. Taxable in all cases
12. Income accrued or deemed to be accrued and received or deemed to be received in India, in not taxable in:
- A. Resident & ordinarily resident
 - B. Resident but not ordinarily resident
 - C. Non resident
 - D. Taxable in all cases
13. An individual shall be deemed to be resident but not ordinarily resident in India if the following conditions are satisfied:
- He is in India for days or more (but less than 182 days) during the previous year and for 365 or more days during 4 previous years immediately preceding the relevant previous year
- A. 120
 - B. 130
 - C. 140
 - D. 150
14. An individual shall be deemed to be resident but not ordinarily resident in India, if following conditions are satisfied: His total income, other than the income from foreign sources, exceeds lakhs during the previous year;
- A. 12
 - B. 13
 - C. 14
 - D. 15
15. If a resident individual satisfies the following two additional conditions, he will be treated as resident & ordinarily resident in India -
- a) He has been resident in India [as per sec. 6(1)] in at least 2 out of 10 previous years immediately preceding the relevant previous year;
 - b) He has resided in India fordays or more during 7 previous years immediately preceding the relevant previous year
- A. 730
 - B. 830

- C. 930
D. 1030

Answers for Self Assessment

1. A 2. D 3. B 4. A 5. B
6. A 7. A 8. C 9. D 10. D
11. D 12. D 13. A 14. D 15. A

Review Questions

1. Explain scope of total Income.
2. What are the guiding principles to decide POEM?
3. When is income deemed to accrue or arise in India?
4. Give 5 example of income which do not form part of total income.
5. Determine the residential status of HUF.



Further Readings

- https://www.icsi.edu/media/webmodules/16112021_Advance_Tax_Laws.pdf
- Income Tax Law & Practice A.Y 2021-22 by Dr H.C. Mehrotra and Dr. S. P. Goyal. Sahitya Bhawan Publications
- Study Material on Direct Tax Laws and International Taxation by ICAI
- Direct Tax Laws and Practice by Dr. Girish Ahuja & Dr. Ravi Gupta

Unit 03: Identification of Residential Status**CONTENTS**

Objectives

Introduction

3.1 General Rule

3.2 Examples of Capital-Related Transactions That are also Explicitly Taxable

3.3 Profit Arising from Sale of Shares and Securities

3.4 A Single Transaction - Can it Constitute Business?

3.5 Liquidated Damages

3.6 Compensation on Termination of Agency/Service Contract

Summary

Keywords

Self Assessment

Answers for Self Assessment

Review Questions

Further Readings

Objectives

After studying this unit, you will be able to:

- Identify the difference between Capital and Revenue Receipts.
- understand the concept of capital and revenue expenditure

Introduction

The courts have repeatedly considered whether a specific receipt represents capital or revenue from a business (*Kettlewell Bullen & Co. Ltd. Vs. CIT* (1964) 53 ITR 261 (SC)). Whether a particular payment should be determined to be chargeable as income under the Income-tax Act or not depends on the facts of each individual case. (1958) 34 ITR 877, *B. Guha & Co. v. CIT* (Punj-Del. Bench). The burden of proof is with the income-tax authorities (*Maharaja Chintamani Saran Nath Sah Deo Vs. CIT* (1971) 82 ITR 464 (SC)), who must demonstrate that there are facts or circumstances that would classify a payment as income.

3.1 General Rule

The general rule under the Income-tax Law is that all revenue receipts are taxable, unless they are specifically granted exemption from tax and all capital receipts are exempt from tax, unless there is a specific provision for taxing them.

Receipts

Can be classified into two kinds: A) Revenue receipt, B) Capital receipt.

Revenue receipts are recurring in nature like salary, profit from business, interest income, etc.

Capital receipts are generally of isolated nature like receipt on account of sale of residential building, personal jewellery, etc.

Criteria for determining whether a receipt is capital or revenue in nature

- Income from transfer of capital asset or trading asset.
- Fixed capital or Circulating capital

Capital Receipts vis-a-vis Revenue Receipts: Tests to be applied

- Transaction entered into the course of business
- Profit arising from sale of shares and securities
- A single transaction - Can it constitute business?
- Liquidated damages
- Compensation on termination of agency/service contract
- Gifts
- It would follow that the spending was of a capital type if it resulted in the creation of an asset or advantage of a lasting nature.
- Even though an expense leads to the production of a capital asset, it will only be considered a revenue expenditure if the capital asset is owned by a third party.
- The expenditure may be regarded as revenue expenditure when it is so closely related to the running or conducting of the business that it can be seen as a crucial step in the process of earning profits rather than for the acquisition of an asset or a right of a permanent nature, the possession of which is a requirement for the running of the business.
- The nature of the trade for which the expense is incurred and its aim, among other factors, are the subject of the transaction that affects the firm.
- When an expense relates to a fixed capital, it may be considered to be of a capital character; but, if the expense relates to circulating capital or stock in trade, it would be considered to be an expense of income.
- Any expenditure made by the assessee in the course of its business to remove any restriction, obstacle, or disability would be on the revenue account if it does not result in the acquisition of any capital assets when the assessee already has the right to operate a business.
- Capital expenditures include payments paid to competing dealers to fend off rivalry in the marketplace. If the cost is a component of operating expenses in routine commercial trade, it is a revenue expenditure rather than a capital one.
- If the expense is made for the initial outlay, an expansion of the firm, or a significant replacement of equipment, it is a capital expenditure; however, if it is made for business operations or is planned as a step in the process of producing a profit, it is revenue in nature.
- If expenses are made to guarantee a consistent supply of raw materials, possibly over a number of years, they go on the revenue account.
- An owner's investment on improvements to a building that increase its worth can be of a capital kind.
- However, if a tenant spends money renovating a rented building, he does not acquire a capital asset because he does not own the building, and often, such spending will be revenue-related.
- The cost of purchasing the company's goodwill would be considered a capital expenditure because it is a capital asset.
- Whether it is paid in one big sum at a time or in instalments over a set length of time would not matter.
- However, if the transaction is for the right to use goodwill rather than its acquisition, the expense would be a revenue expenditure.

Unit 03: Identification of Residential Status

- If the assessee incurs costs in order to create, cure, or complete the title, those costs are considered capital expenditures; but, if they are done so in order to defend the title, they are considered revenue expenditures.

Judgements

- Where the deposit of money is directly linked with the purchase of plant & machinery, any income earned on such deposit is incidental to acquisition of asset and therefore capital in nature (CIT vs. Karnal Co-operative Sugar Mills Ltd. (2000) 14 SITC 578 (SC)).
- Where assessee firm under an agreement sold boilers along with drawings, designs and know-how with further stipulation not to carry out business in the manufacture and design of boilers in future, the receipt on sale of these was held to be of capital nature (Lipi International vs. CIT (2008) 203 Taxation 370 (Bom)).
- The Supreme Court in KCP Ltd. vs. CIT (2000) 245 ITR 421 has held that it is not the name given by the assessee or even the revenue of anyone else that matters, but it is the true character of the receipt that determines its taxability and being regarded as falling within the capital field or out of it.
- The Supreme Court in A.K.T.K.M. Vishnudatta Antharjanam Vs. Commissioner of Agricultural Income-tax (1970) 78 ITR 58 has held that profit motive to not decisive of the question whether a particular receipt is capital or income.
- Supreme Court in CIT Vs. Kamal Behari Lal Singha (1971) 82 ITR 460 has observed one has to see what it is in the hands of the receiver and not its nature in the hands of the payer.
- No matter whether revenue is paid in a lump sum or in instalments, its nature will not change, for example, an employee will receive a salary of rs. 10,000 each month. Instead, he signs a contract to receive a lump sum payment of Rs. 3,60,000 in exchange for three years of service. A revenue receipt is one that contains a lump sum payment or monthly compensation for three years.
- The people receiving the money will decide whether a receipt qualifies as capital or revenue. The place where the money is coming from won't be given any thought. Even if a new business pays salaries using capital, the employees will still receive revenue from it.
- The parties involved may not change the transaction's status as capital or revenue by how they refer to it or how they treat it in the books of accounts.
- Regardless of the amount of capital used in the process, profits from capital that is used up during realization, such as royalties from mines and quarries, are taxable as income.
- The size of the receipt, whether large or small, cannot determine its nature.
- The character of the receipt must be determined at the time of receipt rather than after the recipient has appropriated it.
- It will not matter whether the revenue is earned willingly or as a result of a legal obligation in terms of its nature.
- If a person buys a sculpture to use as interior decoration in his home and subsequently sells it, he will receive a capital gain; yet, if the same sculpture is sold by an art dealer, he will receive a revenue gain.

3.2 Examples of Capital-Related Transactions That are also Explicitly Taxable

1. Capital gains from the disposal of capital assets are defined under Section 2. (14). [Sec. 45]
2. Compensation for service termination or conditions of service change [Section 17(3)]
3. Payments or benefits owing to or received by the individuals listed in section 28(ii)/28 (va).

3.3 Profit Arising from Sale of Shares and Securities

- If the shares were acquired as an investor or with a view to acquiring a controlling interest or for obtaining a managing or selling agency or a directorship, the profit or loss on their sale would be of a capital nature;
- if the shares were acquired in the ordinary course of business as a dealer in shares, it would constitute his stock-in-trade.

3.4 A Single Transaction - Can it Constitute Business?

- Even a single transaction may constitute a business or an adventure in the nature of trade even if it is outside the normal course of the assessee's business.
- Repetition of such transactions is not necessary.

3.5 Liquidated Damages

Receipt of liquidated damages

- directly and intimately linked with the procurement of a capital asset,
- which lead to delay in coming into existence of the profit-making apparatus, is a capital receipt.

CIT v. Saurashtra Cement Ltd. (2010)

- The assessee, a business that manufactures cement, signed a contract with a supplier for the acquisition of a second cement factory.
- One of the terms of the contract stated that if the provider fails to deliver the machinery within the allotted time, assessee will be paid 5% of the cost of the machinery, without evidence of real loss, the corresponding section of the machinery.
- The assessee was given 8.50 lakhs rupees by the way of liquidated damages, the supplier was penalized for failing to deliver the machinery by the deadline.
- The Department determined the liquidated damage amount to be subject to income tax. Nevertheless, the High Court shared the opinion of the Tribunal that the amount was a capital receipt.
- The Supreme Court upheld the High Court's ruling, concluding that the purchase of a capital asset—the cement plant—which caused a delay in the establishment of the profit-making apparatus—was directly and closely related to the losses.
- It wasn't a receipt used in the course of making money.
- As a result, the sum received by the assessee as compensation for sterilising the source of revenue is not in the ordinary course of business and is, in the assessee's hands, a capital receipt.

3.6 Compensation on Termination of Agency/Service Contract

Where an assessee receives compensation on termination of the agency business being the only source of income, the receipt is of capital nature, but taxable under section 28(ii)(c).

However, where the assessee has a number of agencies and one of them is terminated and compensation is received therefor, the receipt would be of a revenue nature since taking up an agency and exploiting the same for earning income is in the ordinary course of business.

Gifts

- Normally, gifts constitute a capital receipt in the hands of the recipient.
- Certain gifts are brought within the purview of section 56(2)(x).

Principles to determine the nature of expense:

- Expenditure on removing the restriction
 - Payment made to the rival dealer to ward off competition in business would constitute capital expenditure
 - If the expenditure is a part of the working expenses in ordinary commercial trading, it is not capital but revenue expenditure.
- The expenditure is incurred for the initial outlay or for extension of business or substantial replacement of equipment; it is capital expenditure.
- The expenditure incurred for ensuring the regular supply of raw materials on the revenue account.
- When an owner incurs expenditure on additions in a building which enhance its value, the expenditure can be of a capital nature.
- But, if a tenant incurs expenditure on a rented building for its renovation, he does not acquire any capital asset because the building does not belong to him and, ordinarily, such expenditure will be of a revenue nature.
- Acquisition of the goodwill of the business is capital expenditure.
- Where, however, the transaction is for the right to use goodwill, the expenditure would be revenue expenditure
- Expenses incurred by the assessee for the purpose of creating, curing or completing the title are capital expenditure, and on the other hand, if such expenses are incurred for the purpose of protecting the same, it is revenue expenditure.

Illustration

- Birla Ltd., a cement manufacturing company, entered into an agreement with a supplier for the purchase of an additional cement plant.
- One of the conditions in the agreement was that if the supplier failed to supply the machinery within the stipulated time, the company would be compensated at 5% of the price of the respective portion of the machinery without proof of actual loss.
- The company received 8.50 lakhs from the supplier by way of liquidated damages on account of his failure to supply the machinery within the stipulated time.
- What is the nature of liquidated damages received by Birla Ltd. from the supplier of the plant for failure to supply machinery to the company within the stipulated time – a capital receipt or a revenue receipt?

Solution

- In the case of CIT -vs.- Saurashtra Cement Ltd. (2010) 325 ITR 422, the Apex Court has held that the damages were directly and intimately linked with the procurement of a capital asset, which led to a delay in coming into existence of the profit-making apparatus.
- It is a capital receipt in the hands of the assessee.

Revenue expenditure is stated in Section 37(1)

“Any expenditure (not being expenditure of the nature described in sections 30 to 36 and not being in the nature of capital expenditure or personal expenses of the assessee), laid out or expended wholly and exclusively for the purposes of business or profession shall be allowed in computing the income chargeable under the head “Profits and gains of business or profession.”

Capital Expenditure

Income Tax Law and Practice

- Capital Expenditure is that expenditure which is incurred for acquiring or bringing into existence an asset or advantage of an enduring benefit.
- Capital expenditure includes not only the purchase price of the fixed asset but also various other expenses incurred in connection with their acquisition.
- For extending or improving a fixed asset or For substantial replacement of an existing fixed asset.
- The benefit of such expenditure is going to accrue for more than one year.

The Examples of Capital Expenditure

Cost of

- land and building,
- plant and machinery,
- furniture and fixtures, etc.

Such expenditure normally yields benefits which extend beyond the current accounting period

Revenue Expenditure

- When the benefit of expenditure is not likely to be available for more than one year, it is treated as revenue expenditure.
- It is incurred to run the business. It does not increase the capacity of the business.
- Usually, the benefit is consumed in the period in which it is incurred except in the case of deferred revenue expense.
- It is taken to the Trading or Profit & Loss Account of the concern.
- Examples: cost of goods purchased, administrative expenses (rent, salary.etc.), manufacturing (oil, fuel, etc.), selling and distribution expenses (discount, advertising, etc.), Depreciation, interest on a loan, loss on sale of assets, etc

Myths about the differentiation between Capital Expenditure and Revenue Expenditure

- Quantum of payment is relevant for determining whether an expenditure is a Revenue or Capital
- Universal application of the concept of enduring benefit:
- Fixed and circulating Capital test:

CIT vs. Coal Shipment Pvt

- In the case of CIT vs Coal Shipment Pvt. Ltd, the Hon'ble Supreme Court held that "Although payments made to eliminate competition in business, to a rival dealer would constitute capital expenditure if the object of making that payment is to derive an advantage by eliminating the competition over some length of time, the same result would not follow if there is no certainty of the duration of the advantage and the same can be put to an end at any time.
- A benefit need not be of an everlasting character, but it should not be so short-lived that it can be terminated at any time at the will of any of the parties.

Lakshmi ji Sugar Mills 1971

- Also, in the case of Lakshmi Ji Sugar Mills 1971, it was decided that wherein expenditure incurred on construction and development of roads between sugarcane producing centres and sugar factories was held to be revenue in nature as it was incurred for the purposes of facilitating running of the assessee motor vehicles etc.

Fixed and circulating Capital test:

Unit 03: Identification of Residential Status

- Fixed capital is what the owner turns to profit by keeping it in his possession; circulating capital (labor, raw material, power etc.) is what the assessee makes profit by parting or letting the product/asset change masters/hands. This test could be applied when the acquisition of an asset clearly falls within one of the two categories, but the test would break down where the expenditure does not fall easily within the specified category.
- The demarcation line between assets, out of which profits were earned and the profit made upon assets or with assets, was thin and difficult to draw in several cases.

Empire Jute Company (Supra),

- In the case of Empire Jute Company (supra), the assessee company was carrying on the business of manufacturing jute and was a member of the Indian Jute Mills Association.
- The assessee purchased "loom hours" from four other mills for an aggregate amount of Rs.2,03,255/- and claimed those expenditures as revenue expenditure.

Decisive tests of demarcations between Capital Expenditure and Revenue expenditure as indicated by various courts

- Every case has to be decided on its own facts keeping in mind the broad picture of the whole operation in respect of which the expenditure has been incurred.
- The tests are thus mutually exclusive and have to be applied to the facts of each particular case in a rational manner.
- If the expenditure is made for acquiring or bringing into existence.
- It is the aim and object of expenditure which would determine its character and not the source and manner of its payment
- In applying the test of an advantage of an enduring nature, it would not be proper to look at the advantage obtained as lasting forever.

If the expenditure is made for acquiring or bringing in to existence

- In the case of Commissioner of Income Tax v. Madras Auto Services (P) Ltd. (1998) 233 ITR 468 (SC), the assessee had incurred expenditure on demolishing the existing building and constructing a new building at their own expense.
- The new building belonged to the lessor and the assessee remained a lessee but at a low rent.
- Term for lease was 39 years, but the Supreme Court held that the expenditure was revenue in nature as the newly constructed property from the beginning was owned by the lessor.

Aim and Object of Expenditure

- In the case of Mascon Technical Services Ltd. v. CIT (2013) 358 ITR 545 (Mad), the High Court's Decision:
- The High Court noted that the assessee-company had taken steps to go in for a public issue and incurred share issue expenses for the same.
- However, it could not go in for the public issue by reason of the orders issued by the SEBI just before the proposed issue.
- The expenditure, therefore, constitutes a capital expenditure.

In applying the test of an advantage of an enduring nature, it would not be proper to look at the advantage obtained, as lasting forever.

- In the case of Mohan Meakin Breweries Ltd. V. Commissioner of Income Tax, (1997), the High Court has held that payment made to the State towards license fee or permit under the provisions of Punjab Excise Act and Punjab Distilleries Rules applicable to the State of Himachal Pradesh, was capital expenditure.

Income Tax Law and Practice

- However, the expenditure incurred for operating or running of distillery would not be capital expenditure as it relates to and is a part of the operational expenses.

An expenditure which enables the profit-making structure to work more efficiently

- An expense incurred for the acquisition of a source of profit or income would, in the absence of any contrary circumstance, be in the nature of capital expenditure.
- As against this, an expenditure that enables the profit-making structure to work more efficiently, leaving the source or the profit-making structure untouched would be in the nature of revenue expenditure.

Expenditure Incurred for Grant of Licence

Expenditure incurred for grant of licence which accord "access" to technical knowledge, as against "absolute" transfer of technical knowledge and information would ordinarily be treated as revenue expenditure.

In order to sift (examine thoroughly), in a manner of speaking, the grain from the chaff (sort the valuable thing from the worthless), one would have to closely look at the attendant circumstances such as

- a) The tenure of license
- b) The right, if any, in the licensee to create further rights in favour of third parties,
- c) The prohibition, if any, in parting with a piece of confidential information received under the license to third parties without the consent of the licensor,
- d) Whether on expiry of the license the licensee is required to return back the plans and design obtained under the license to the licensor even though the licensee may continue to manufacture the product, in respect of which „access“ to knowledge was obtained during the subsistence of the license, Advertisement
- e) Expenditure on obtaining access to such a secret process would ordinarily be construed as capital in nature

Test enunciated by courts have to be applied from a business Point of view

- While determining the nature of expenditure, given the diversity of human affairs and complicated nature of business;
- the test enunciated by courts has to be applied from a business point of view and on a fair appreciation of the whole fact situation before concluding whether the expenditure is in the nature of capital or revenue.

Summary

Revenue expenditures are admissible as expenses until specifically prohibited by the Act, while capital expenditures are not, unless specifically permitted by the Act. In conclusion, "whether a given expenditure is "revenue or capital" must be judged on the basis of all the facts and circumstances and by the application of rules as established by several decided instances. The issue must be considered in the broader framework of commercial necessity or expediency.

Keywords

Payment has actually been made: Regardless of the prior year in which the responsibility for the expenditure was incurred in accordance with the assesses ordinary way of accounting, or payable in such a manner as may be prescribed, "payment has actually been made" refers to the actual payment of the expenditure.

Circulating capita: as what he makes profit of by parting with it and letting it change masters

Fixed capital: as what the owner turns to profit by keeping it in his own possession

Self Assessment

1. Replacement of the carpets, is revenue/Capital expenditure? -It was held:
 - A. Renovation in hotels-carpets in the hotel business require frequent changes. They are in the nature of capital asset, thus the expenditure incurred on such assets for the replacement of the carpets, is revenue expenditure
 - B. Renovation in hotels-carpets in the hotel business require frequent changes. They are not in the nature of capital asset, thus the expenditure incurred on such assets for the replacement of the carpets, is capital expenditure
 - C. Renovation in hotels-carpets in the hotel business require frequent changes. They are not in the nature of revenue expense, thus the expenditure incurred on such assets for the replacement of the carpets, is capital expenditure
 - D. Renovation in hotels-carpets in the hotel business require frequent changes. They are not in the nature of capital asset, thus the expenditure incurred on such assets for the replacement of the carpets, is revenue expenditure

2. Which of the following is wrong in regard to Market survey-expenditure?
 - A. Market survey-expenditure incurred on the market survey is revenue expenditure.
 - B. Assessee, a manufacturer of a soft drink having conducted a market research by using the services of a professional agency to determine its brand performance with price, gauge the consumer demand at the current price or a lower price and to know whether its brand can adopt a different pricing between the base flavors and the new flavors, the expenses were incurred for exploring the circumstances as to how assessee can carry on its business more potentially and not exploring the market of a new product and, therefore, same is allowable as revenue expenditure.
 - C. The decision in Priya Village Road Show, in this Court's opinion, is distinguishable. In that case, the existing business was sought to be expanded, and the market survey commissioned by the assessee was to get consumer feedback about its brand strength and performance. In this case, however, the market survey appears to be of a different kind. These expenses, in the court's opinion (joint venture share reimbursement, joint venture agreement drafting fee, market survey report fees) are pre-startup expenses in respect of an aborted activity, which would fall within the proscribed category spelt out in Challapalli Sugars Ltd. V Commissioner of Income-tax (1975) 98 ITR 167 (SC).
 - D. In Cit vs Hindustan Times on 14 September, 2012 sum of Rs. 5,76,975/-, paid to IMRB for market research on life insurance business in India, was not a deductible expenditure.

3. Which of the following is wrong in respect to their judgements?
 - A. Employee Stock Option Plan: difference between the market value and issue price of the share, is revenue expenditure - CIT v. PVP Ventures Ltd. [2012]
 - B. In CIT Vs PVP Ventures Limited (Madras High Court), it was held The allotment of shares was done by the assessee in strict compliance of SEBI regulations, which mandate that the difference between the market prices and the price at which the option is exercised by the employees is to be debited to the Profit and Loss Account as an expenditure.
 - C. In M/S Novozymes South Asia Pvt Ltd , ... vs Assistant Commissioner Of Income ... on 29 June, 2021 it was held difference between the grant price and the market price on the shares as on the date of grant of options is allowable as a deduction under section 37 of the Act.

- D. Companies are not allowed to make tax-deductible contributions to the ESOP to buy out the shares or the company can use the ESOP to borrow money to buy the shares.
4. Which of the following statements is wrong?
- A. Royalty paid under a 5-year collaboration agreement for use of technical know-how to run an existing business more profitability would be allowable as capital expenditure - CIT v. Southern Pressing (P). Ltd. [2000] 242 ITR 67(Mad.).
- B. Registration Fees- Registration fee paid by the company assessee for increasing in the authorised share capital, is the capital expenditure Bharat Carbon & Ribbon Mfg Co. Ltd. v. CIT [1981] 127 ITR 239 (Delhi) [approved in Punjab State Industrial Development Corporation corporation Ltd. v. CIT[1997] 93 Taxman 5 (SC).
- C. Interest on delayed payments for purchase of machinery is allowable as a revenue expenditure-CIT v. Sivakumari Mills Ltd.[1997] 227 ITR 465/95 Taxman 73(SC).
- D. Where the assessee, by paying damages to the preference shareholders is actually discharging its liability to pay dividend under the contract, such kind of payments cannot be allowed as business expenditure.-G.G.L.Hotels & resorts Co.Ltd v. CIT [2017] 82 taxmann.com 107/390 ITR 160(Cal.)
5. Which of the following statements is wrong?
- A. Commission paid at a higher rate in order to attract first customer in a new region is deductible-CIT v. Bharat Collieries Ltd.[1968] 68 ITR 42(Pat.).
- B. Payment made under know-how agreement to use technical know-how and trademark is not allowable as revenue expenditure and merely because the agreements provided that the assessee shall be entitled to retain the technical know-how design, drawings etc even after the termination of the agreement, it will alter the nature of the transaction-Praga Tools Ltd. v. CIT[1980] 123 ITR 773(AP).
- C. Litigation expenses incurred to defend a suit filed by the shareholder where, it relief was granted by it would have affected the carrying on the assessee's business, are deductible - Premire Construction Co. Ltd. v. CIT[1966] 62 ITR 176 (Bom.).
- D. Money spend by a partner in a suit against another partner for rendition of accounts is not an allowable deduction
6. Which of the following statements is wrong?
- A. Taxes: General rule- Any tax (other than income tax, gift tax, fringe benefits tax, dividend tax, surtax) is not allowed as deduction if it is paid /payable while carrying on the business and profession subject to the section 43B.
- B. Municipal taxes paid by a running concern on plot purchased by it for business purposes is deductible even if the building is not constructed-CIT v. Suri Sons [1989] 177 ITR 406 (Punj.& Har.).
- C. Professional tax paid by a person carrying on business or trade is deductible-Circular No.16, dated September 18, 1969.
- D. Contribution to an association, which does not serve any business purpose, -Iron traders(P) Ltd. v. CIT[1974] 97 ITR 606(Delhi).
7. Which of the following statements is wrong?
- A. Contribution to insurance Fund can be considered as an admissible deduction-CIT v. Thanthai Preiyar Transport Corporation.

Unit 03: Identification of Residential Status

- B. where loss is incurred by the company-assessee due to fluctuation of exchange rates in remittances of profit from India to its U.K office, it is allowed as deduction-Goodricke Groups Ltd. (No.2) v. CIT[1993] 201 ITR 266 (Cal.)
- C. if an society assessee as a corporate body make a decision to give presents to its members to celebrate silver jubilee celebration, the expenditure on such expenditure on such presents is allowable as deduction-Karjan Co-operative cotton sales Ginning & pressing society v. CIT [1993] 199 ITR 17 (Guj.)(FB).
- D. Expenditure on Diwali Gifts is allowable as business expenditure - CIT v. Anil Alums (P.) Ltd. [2005] 98 TTJ (Asr.) 56.
8. Which of the following statements is wrong?
- A. Premium paid by the firm in respect of the life of its partners, assured under Keyman insurance policy - P.G Electronics v. ITO [2007] 15 SOT 79 (Delhi)(SMC)(URO) circular no.38/2016,dated November 22,2016, CBDT has admitted that premium paid by a firm on the Keyman Insurance policy of a partner, not to safeguard the firm against a disruption of a business,is allowed as deduction under section 37.
- B. Just because Keyman Insurance Policy is assigned by the company to its director after sometime will not mean that expenditure incurred in first instance will lose flavour of it being "business expenditure"-CIT v. Rajan Nanda [2012] 205 taxmen 138/18 taxmann.com 98 (Delhi).
- C. Premium paid by the firm in respect of the life of its partners,assured under Keyman insurance policy - P.G Electronics v. ITO [2007] 15 SOT 79 (Delhi)(SMC)(URO) circular no.38/2016,dated November 22,2016, CBDT has admitted that premium paid by a firm on the Keyman Insurance policy of a partner, to safeguard the firm against a disruption of a business,is not allowed as deduction under section 37.
- D. Just because Keyman Insurance Policy is assigned by the company to its director after sometime will mean that expenditure incurred in first instance will loose flavour of it being "business expenditure"-CIT v. Rajan Nanda [2012] 205 taxman 138/18 taxmann.com 98 (Delhi).
9. Which of the following is not allowed as deduction?
- A. Expenses on legal proceedings under any law incurred in connection with Business
- B. Penalty for breach of law
- C. Penalty for breach of contract
- D. Interest under any other law provided not for breach of law.
10. Which of the following is not allowed as deduction?
- A. Professional Tax paid in carrying on business or trade Allowed
- B. Diwali & muhurat expenses Allowed
- C. Deposit under acquiring a telephone
- D. Interest on loan taken to pay Income Tax
11. Which of the following statements is wrong?
- A. Legal expenses incurred in defending a suit for breach of contract to supply goods is a revenue expenditure as the expenses have been incurred for carrying on the business.
- B. Legal expenses incurred in defending a suit for breach of contract to supply goods is a revenue expenditure as the expenses have been incurred not for carrying on the business.

Income Tax Law and Practice

- C. Legal expenses incurred in defending a suit for breach of contract to supply goods is a capital expenditure as the expenses have been incurred not for carrying on the business.
- D. Legal expenses incurred in defending a suit for breach of contract to supply goods is a capital expenditure as the expenses have been incurred for carrying on the business.
12. Which of the following statements is wrong?
- A. A second-hand car was purchased for a sum of r 40,000. A sum of 10,000 was spent on its overhauling. Here 50,000 is treated as capital expenditure since overhauling makes the asset ready for use.
- B. A second-hand car was purchased for a sum of r 40,000. A sum of 10,000 was spent on its overhauling. Here only 40,000 is treated as capital expenditure since overhauling makes the asset ready for use.
- C. A second-hand car was purchased for a sum of r 40,000. A sum of 10,000 was spent on its overhauling. Here only 10,000 is treated as capital expenditure since overhauling makes the asset ready for use.
- D. A second-hand car was purchased for a sum of r 40,000. A sum of 10,000 was spent on its overhauling. Here 30,000 is treated as capital expenditure since overhauling makes the asset ready for use.
13. Which of the following statements is wrong?
- A. Legal expenses incurred for the issue of debentures are a capital expenditure because the expenditure is incurred for obtaining the capital of the company.
- B. Legal expenses incurred for the issue of debentures are a revenue expenditure because the expenditure is incurred for obtaining the capital of the company.
- C. Legal expenses incurred for the issue of debentures are a capital expenditure because the expenditure is incurred not for obtaining the capital of the company.
- D. Legal expenses incurred for the issue of debentures are a revenue expenditure because the expenditure is incurred not for obtaining the capital of the company.
14. Which of the following statements is wrong?
- A. Legal expenses to purchase land is a revenue expenditure since they constitute the cost of a fixed asset.
- B. Legal expenses to purchase land is a capital expenditure since they do not constitute the cost of a fixed asset.
- C. Legal expenses to purchase land is a revenue expenditure since they do not constitute the cost of a fixed asset.
- D. Legal expenses to purchase land is a capital expenditure since they constitute the cost of a fixed asset.
15. Which of the following statements is wrong?
- A. Legal expenses to defend infringement of trademarks is capital expense as these are incurred to maintain a fixed asset.
- B. Legal expenses to defend infringement of trademarks is capital expense as these are not incurred to maintain a fixed asset.
- C. Legal expenses to defend infringement of trademarks is revue expense as these are incurred to maintain a fixed asset.

- D. Legal expenses to defend infringement of trademarks is revenue expense as these are not incurred to maintain a fixed asset.

Answers for Self Assessment

- | | | | | |
|-------|-------|-------|-------|-------|
| 1. D | 2. D | 3. D | 4. A | 5. B |
| 6. A | 7. A | 8. B | 9. B | 10. D |
| 11. A | 12. A | 13. A | 14. D | 15. C |

Review Questions

1. Comment on the nature of receipts that are taxable.
2. What is the difference between capital and revenue receipt?
3. What is the difference between capital and revenue expenditure?
4. All revenue receipts are taxable, unless they are specifically granted exemption from tax. Give examples of these specific exemptions
5. All capital receipts are exempt from tax, unless there is a specific provision for taxing them. Give examples of these specific taxation provisions.



Further Readings

- https://www.icsi.edu/media/webmodules/16112021_Advance_Tax_Laws.pdf
- Income Tax Law & Practice A.Y 2021-22 by Dr H.C. Mehrotra and Dr. S. P. Goyal. Sahitya Bhawan Publications
- Study Material on Direct Tax Laws and International Taxation by ICAI
- Direct Tax Laws and Practice by Dr. Girish Ahuja & Dr. Ravi Gupta

Unit 04: Computation of Income under the Head Salaries

CONTENTS

Objectives

Introduction

4.1 Basic Elements of Salary

4.2 Definition Of Salary [SEC. 17(1)]

4.3 Basis of Charge [SEC. 15]

4.4 Place of Accrual of Salary

4.5 Computation of Salary, At A Galance

4.6 Allowances

4.7 Perquisites: Meaning and Chargeability

Summary

Keywords

Self Assessment

Answers for Self Assessment

Review Questions

Further Readings

Objectives

After studying this unit, you will be able to:

- understand the concept of salary, profits in lieu of salary.
- identify the point of time when salary income is taxable.
- determine the taxable portion of retirement benefits.
- understand the concept of allowances.
- identify the allowances which are exempt from tax.
- understand the concept of perquisites.
- identify the tax-free perquisites.
- determine the value of perquisites that are taxable under the head "Salaries".

Introduction

The chargeability of a person's income under the Income Tax Act of 1961 determines whether or not it is taxable. Section 4 charges tax on an assessee's whole income (subject to statutory exemptions) (1). Section 5 defines the range of total income, which changes based on residence status. The heads of income listed in Section 14 are those that an assessee's income will fall under. Various sections of the Act cover the guidelines for calculating income and the permitted deductions under various heads of income. For the purpose of calculating income, the following are the heads of income and the accompanying set of sections: Sections 15 to 17 deal with salaries; Sections 22 to 27 deal with income from real estate; Sections 28 to 44D deal with business and profession profits; Sections 45 to 55A deal with capital gains; and Sections 28 to 44D deal with income from other sources (Sections 56 to 59). Students will grasp how to compute income under head salaries, what deductions are allowed, and what salary exemptions are available after completing this session.

4.1 Basic Elements of Salary

- Employer and employee (or Master & Servant) relationship; and
- Payment must have been made by the employer in such capacity

4.2 Definition Of Salary [SEC. 17(1)]

As per sec. 17(1) of the Income-tax Act, 1961, salary includes the following:

- Wages;
- Any annuity or pension;
- Any gratuity;
- Any fees, commission, perquisite or profits in lieu of or in addition to any salary or wages;
- Any advance of salary;
- Any payment received in respect of any period of leave not availed of by the assessee;
- The portion of the annual accretion in any previous year to the balance at the credit of an employee, participating in recognised provident fund, to the extent it is taxable;
- Transferred balance in a Recognised Provident Fund to the extent it is taxable.
- Contribution made by the employer in the previous year to the account of an employee under a pension scheme referred to in sec. 80CCD [National Pension Scheme and Atal Pension Yojana].

4.3 Basis of Charge [SEC. 15]

- Advance salary (on 'receipt' basis)
Advance salary is taxable u/s 17(1)(e) whereas 'Advance against salary' is treated as loan hence, not taxable under the head "Salaries".
- Outstanding salary (on 'due' basis)
- Arrear salary (on 'receipt' basis)

4.4 Place of Accrual of Salary

Salary which is received in India or earned in India shall be taxable in the hands of all assesseees, whether resident or non-resident in India. Salary is deemed to be earned in India provided --

- The service is rendered in India;
- The rest period or leave period, which is preceded and succeeded by the service rendered in India and forms part of the service contract of employment.

Exceptions:

- Salary paid to a Government employee, being a citizen of India, is deemed to accrue in India, irrespective of place of work [Sec. 9(1)(iii)].
- Pensions payable outside India to certain categories of Government employees and Judges who permanently reside outside India shall not be deemed to arise or accrue in India. [Sec. 9(2)]

4.5 Computation of Salary, At A Glance

Basic Salary

Fees

Commission

Unit 04: Computation of Income under the Head Salaries

Bonus

Gratuity

Leave Encashment

Pension

Retrenchment Compensation

Compensation received under Voluntary Retirement Scheme

Allowances:

- Dearness Allowance (DA) /Dearness Pay (DP) House Rent Allowance
- Children Education Allowance
- Children Hostel Allowance
- Entertainment Allowance
- Medical Allowance
- Conveyance Allowance
- City Compensatory Allowance
- Uniform Allowance
- Professional Development Allowance Transport Allowance
- Other Allowances

Perquisites u/s 17(2)

- Any Obligation of Employee paid by Employer Accommodation
- Shares and securities issued under ESOP Employer's Contribution to Superannuation Fund
- Gas, Electricity & Water
- Medical Facility
- Other fringe benefits

Leave Travel Concession

Contribution of Employer to Provident Fund

Interest on Recognised Provident Fund

Any other item

Gross Salary

Less: Deduction u/s 16 (ia)

- i. Standard Deduction
- ii. Entertainment Allowance
- iii. Tax on employment/Professional tax

Taxable Salary

Treatments

- Basic Salary: It is the sum paid by the employer to an employee as salary and shall be fully taxable.
- Pay-Scale (Grade system): It is a system of payment where the increment scale is pre-known to the employee.
 - E.g. Basic salary is given as 10,000 – 1,000 – 13000 – 2,000 – 18,000.
- Dearness Allowance (DA) or Dearness Pay (DP): It is an extra amount given to an employee to meet the burden of inflation or increased cost of living. This is fully taxable.
- Fees:

- An employee may be given, apart from a basic salary, extra remuneration for doing a specific job under the terms of employment. Such extra remuneration is termed as fee and shall be fully taxable.
- Commission: It may be as a percentage of turnover or as a percentage of profit. In either case, it is taxable.
- Bonus: Bonus may be contractual or voluntary. In either case, it is fully taxable
- Gratuity
 - Case A: Gratuity received during the continuation of service
 - Case B: Gratuity received at the time of termination of service by a Government employee
 - Case C: Gratuity received at the time of termination of service by non-government (including foreign government) employee, covered by the Payment of Gratuity Act. In such case, a minimum of the following shall be exempted from tax u/s 10(10) (ii):
 1. Actual Gratuity received;
 2. ₹ 20,00,000; or
 3. 15 working days salary for every completed year of service [Arithmetically, $15/26 \times$ Completed year of service \times Salary p.m.]
- Notes:
 - a) Completed year of service includes any fraction in excess of 6 months. (e.g. 7 years 9 months will be treated as 8 years; 7 years 5 months will be treated as 7 years and 7 years 6 months will be treated as 7 years).
 - b) Salary here means Basic + DA, last drawn

In case of an employee of a seasonal establishment: 15 days shall be replaced by 7 days. (i.e., $7/26 \times$ Completed year of service \times Salary p.m.)

In case of a piece-rated employee: 15 days' salary would be computed on the basis of the average of total wages (excluding wages paid for overtime) received for a period of 3 months immediately preceding the termination of his employment.
- Case D: Gratuity received at the time of termination of service by the non-government employee (including foreign government employee) is not covered under the Payment of Gratuity Act
- Exempted from tax u/s 10(10)(iii) to the extent of lower of the following:
 1. Actual Gratuity received;
 2. ₹ 20,00,000; and
 3. $1/2 \times$ Completed year of service \times Average Salary p.m.
- Case E: Shall not be taxable in the hands of the recipient

Leave Salary Encashment

- Case A: Leave salary received during the continuation of service (
 - Fully Taxable
- Case B: Leave salary received by Government employee on termination of service
 - Fully exempted u/s 10(10AA)(i)
- Case C: Leave salary received by a non-Government employee on termination of service

Exempted to the minimum of the following u/s 10(10AA)(ii):

 - a) Actual amount received as leave salary
 - b) ₹ 3,00,000/-
 - c) $10 \times$ Average salary p.m.

Unit 04: Computation of Income under the Head Salaries

d) To the maximum of 30 days (normally taken as 1 month) average salary¹ for every completed year of service², subject to deduction for actual leave availed during the tenure of service

- Case D: Leave salary paid to the legal heir
 - Not taxable.

Pension [SEC. 17(1)(ii)]

- Case A: Uncommuted pension Fully-taxable in the hands of all employees, whether Government or Non -Government employees.
- Case B: Commuted pension received by a Government Employee Fully exempt from tax u/s 10(10A) (i).
- Case C: Commuted pension received by an employee who also received gratuity [Sec. 10(10A) (ii)]: One-third of the total pension (which assessee is normally entitled to) commuted is exempt.
- Case D: Commuted pension received by an employee who does not receive gratuity [Sec. 10(10A) (ii)] One-half of total pension (which assessee is normally entitled to) commuted is exempt

Retrenchment Compensation

Exempted to the extent of a minimum of the following:

- Actual amount received;
- ₹ 5,00,000; or
- An amount calculated in accordance with the provisions of sec. 25F(b) of Industrial Dispute Act, 1947 (Under the said Act, a workman is entitled to retrenchment compensation equivalent to 15 days' average pay for every completed year of service or any part thereof in excess of 6 months).

Annuity [SEC. 17(1)(ii)]

Annuity means a yearly allowance, income, grant of an annual sum, etc., for life or in perpetuity.

Case A: Annuity payable by a present employer, whether voluntarily or contractual:

Fully taxable as salary

Case B: Annuity received from an ex-employer

Fully taxable as 'profit in lieu of salary' u/s 17(3)(ii)

Case C: Annuity received from a person other than the employer, e.g. from the insurer, etc.

Taxable as per provision of Sec. 56 as 'Income from other sources.'

Compensation Received At The Time Of Voluntary Retirement [SEC. 10(10C)]

Amount of exemption shall be a minimum of the following -

- Actual amount received as per guidelines; or
- ₹ 5,00,000

Specified Employer

- Any company; or an authority established under Central, State or Provincial Act; or A local authority; or A Cooperative society; or A Specified University; or an Indian Institute of Technology (IIT); or Any State Government; or The Central Government; or Notified Institution of Management (IIM Ahmedabad, IIM Bangalore, IIM Calcutta, IIM Lucknow, and the Indian Institute of Foreign Trade New Delhi); or Notified Institution.
- The amount of compensation does not exceed
 - the amount equivalent to 3 months' salary for each completed year of service;

- salary at the time of retirement multiplied by the balance month of service left.
- Note: Salary here means [Basic + DA (if forms a part of retirement benefit) + fixed percentage of commission on turnover], last drawn

Salary Received In Lieu Of Notice Period:

- Fully taxable.

Profits In Lieu Of Salary [SEC. 17(3)]

- Following receipts are taxable as profits in lieu of salary:
- The amount of any compensation due to or received by an assessee from his employer or former employer at or in connection with the (a) termination of his employment, (b) modification of the terms and conditions of employment.
 - Any payment due to or received by an assessee from his employer or former employer except the following:
 - Gratuity exempted u/s 10(10);
 - House rent allowance exempted u/s 10(13A);
 - Commuted pension exempted u/s 10(10A);
 - Retrenchment compensation exempted u/s 10(10B);
 - Payment from an approved Superannuation Fund u/s 10(13);
 - Payment from statutory provident fund or public provident fund;
 - Payment from recognised provident fund to the extent it is exempt u/s 10(12).

Any payment from the unrecognised provident fund or such other fund to the extent to which it does not consist of contributions by the assessee or interest on such contributions.

Any sum received by the employee under the Keyman Insurance Policy, including the sum allocated by way of bonus on such policy.

Any amount due to or received by the employee (in a lump sum or otherwise) prior to employment or after cessation of employment.

4.6 Allowances

- Exempted Allowances
- General Allowance
- Allowance u/s 10(14)(i), deductions from which depend upon actual expenditure [Rule 2BB(1)]
- Allowance u/s 10(14)(ii), deductions from which do not depend upon actual expenditure [Rule 2BB(2)]

Exempted Allowances

- Allowances to a Government employee being an Indian citizen working outside India [Sec. 10(7)]
- Allowances received from UNO
- Compensatory allowance under Article 222(2) of the
- Constitution Allowance to judges of the High Court and the Supreme Court
- Allowances to teacher / professor from the SAARC Member States Any other Allowance

Allowances, deduction from which depends on actual expenditure [Sec. 10(14)(i)]

- Travel or transfer Allowance
- Daily Allowance
- Conveyance Allowance
- Helper / Assistant Allowance

Unit 04: Computation of Income under the Head Salaries

- Research Allowance
- Uniform Allowance

Allowances, deduction from which depends on actual expenditure [Sec. 10(14)(i)]

- Children Education Allowance
- Children Hostel Allowance
- Truck Driver's Allowance
- Transport Allowance
- Tribal Areas Allowance,
- Special Compensatory Allowance,
- Border Area Allowance, etc.

Treatment

Minimum of the following shall be exempted:

- a) Actual amount received; or
- b) Actual expenditure incurred for such purpose

Children Education Allowance

Minimum of the following is exempted from tax –

- a. 100 per month per child (to the maximum of two children)
- b. Actual amount received for each child (to the maximum of two children)

Children Hostel Allowance

Treatment:

Minimum of the following is exempted from tax –

- a) 300 per month per child (to the maximum of two children)
- b) Actual amount received for each child (to the maximum of two children)

Truck Driver Allowance

Treatment:

Minimum of the following shall be exempted:

- a. 70% of the allowance.
- b. 10,000 p.m.

Taxpoint:

If the assessee is in receipt of the Daily allowance, then above allowance shall be fully taxable.

Transport Allowance

- An allowance, by whatever name called, to meet the expenditure for the purpose of travelling between the place of residence and the place of duty.
- Available to: Assessee is blind / deaf and dumb / orthopedically handicapped.

Treatment:

Minimum of the following shall be exempted:

- Actual amount received; or
- 3,200 p.m.

Allowance to Government employees outside India

As per sec. 10(7), any allowance or perquisite allowed outside India by the Government to an Indian citizen for rendering services outside India is wholly exempt from tax.

Allowance received from UNO (United Nations Organization)

Income Tax Law and Practice

Basic salary or Allowance paid by the UNO to its employees are not taxable.

Compensatory Allowance

Under Article 222(2) of the Constitution It is fully exempt from tax

Allowance to judges of the High Court or the Supreme Court

- Any allowance paid to Judges of the High Court u/s 22A(2) and sumptuary allowance u/s 22C of the "High Court Judges (Conditions of Service) Act, 1954" is not taxable. Allowance to the Supreme Court Judges u/s 23B of the "Supreme Court Judges (Conditions of Service) Act, 1958" is also exempt.

Salary to teacher or professor from SAARC Member States [DTAA]

Salary including allowances and perquisites of a teacher or professor or research scholars from SAARC Member States shall not be taxable if the following conditions are satisfied:

Salary to teacher or professor from SAARC Member States [DTAA]

1. Such professor, teacher, or research scholar is a resident of other SAARC member States (i.e., Bangladesh, Bhutan, India, Maldives, Nepal, Pakistan & Sri Lanka) prior to visiting another member State.
2. Such visit is for the purposes of teaching or engaging in research or both at a university or college or similar approved institution in that other Member State.
3. The remuneration from aforesaid activities in other Member State is exempt for a period of 2 years from the date of arrival in the other member State.

House rent allowance (HRA) [Sec. 10(13A) and rule 2A]

Minimum of the following is exempted from tax:

- a. Actual HRA received.
- b. An amount equal to 50% of salary (when house is situated in a metro city) or 40% of salary¹ (when house is situated in any other place) for the relevant period
- c. The excess of rent paid over 10% of salary.

Salary here means: Basic + D.A. (if it forms a part of retirement benefit) + Commission as a fixed % on turnover

Travel or transfer Allowance

An allowance, by whatever name called, to meet the cost of travel on tour. Cost of travel includes any sum paid in connection with transfer, packing, and transportation of personal effects on such transfer

Illustration 1

Basic Salary	2000	12	24000
Dearness Allowance	3000	12	36000
Dearness Pay	1000	12	12000
Fees	50000p.a.		50000
House Rent Allowance	4167	12	50000
Children Education allowance	3000	12	36000
Children allowance	1000	12	12000
Hostel allowance	2000	12	24000

Unit 04: Computation of Income under the Head Salaries

Dress Allowance	5000	12	60000
Uniform Allowance	2000	12	24000
Tiffin Allowance	2000	12	24000
Education Allowance for her own education	2000	12	24000

Additional Information:

Uniform:

Actual expenditure 1000 p.m.

Education Allowance for her own education:

Actual expenditure 1,500 p.m

Dress Allowance:

Actual expenditure 10,000 p.m.

- She is having one adopted child
- Rent paid for Kolkata house 4,000 p.m.

Solution

Basic Salary		24000
Fees		50000
Allowances		
Dearness Allowance		36000
Dearness Pay		12000
House Rent Allowance		14,000
Children Education Allowance		34,800
Children Allowance		12,000
Hostel Allowance		20,400
Dress Allowance (fully taxable)		60000
Uniform Allowance		12000
Tiffin Allowance		24000
Education Allowance for her own education		6000
Gross salary		305200

Taxable Children Education Allowance:

- Children Education Allowance 36,000
- Less: Exemption (100 x 1 x 12) (1,200)
- Taxable: 34,800

Taxable Hostel Allowance

- Hostel Allowance: 24000

Income Tax Law and Practice

- Less:Exempted: $300 \times 1 \times 12 = (3600)$
- Taxable: 20400

TaxableUniform Allowance

- Uniform Allowance: 24000
 - Less:Exempted: $1000 \times 12 = (12000)$
- Taxable: 12000

TaxableEducation Allowance

- Education Allowance: 24000
 - Less:Exempted: $1500 \times 12 = (18000)$
- Taxable 6000

House Rent Allowance 50,000

- Less:
- Minimum of the following u/s 10(13A)
 - Actual Amount Received: 50,000
 - 50% of Salary
 - i.e. 50% of $(24,000 + 36,000 + 12,000)$: 36,000
 - Rent Paid - 10% of Salary $(48,000 - 7,200)$: 40,800
- Exemption: 36,000
- Taxable: 14,000

Basic Salary		24000
Fees		50000
Allowances		
Dearness Allowance		36000
Dearness Pay		12000
House Rent Allowance		14,000
Children Education Allowance		34,800
Children Allowance		12,000
Hostel Allowance		20,400
Dress Allowance (fully taxable)		60000
Uniform Allowance		12000
Tiffin Allowance		24000
Education Allowance for her own education		6000
Gross salary		305200

Fully Taxable Allowance

Unit 04: Computation of Income under the Head Salaries

- City Compensatory Allowance
- Tiffin Allowance
- Medical Allowance an allowance to meet the expenditure on medical treatment etc.
- Servant Allowance
- Non-practicing Allowance
- Warden or Proctor Allowance
- Deputation Allowance
- Entertainment Allowance

4.7 Perquisites: Meaning and Chargeability

As per sec. 17(2) of the Income tax Act, Perquisite includes –

- i. Value of rent-free accommodation provided by the employer.
- ii. Value of concession in rent in respect of accommodation provided to the assessee by his employer.
- iii. The value of any benefit or amenity granted or provided free of cost or at concessional rate to 'specified employees'.
- iv. Amount paid by an employer in respect of any obligation which otherwise would have been payable by the employee.
- v. Sum payable by an employer, whether directly or through a fund other than recognised provident fund or approved superannuation fund or deposit-linked insurance fund, to effect an assurance on the life of the assessee or to effect a contract for an annuity.
- vi. The value of any specified security or sweat equity shares allotted or transferred, directly or indirectly, by the employer, or former employer, free of cost or at concessional rate to the assessee.
- vii. The amount or the aggregate of amounts of any contribution made to the account of the assessee by the employer:
 - i. in a Recognised Provident Fund (RPF);
 - ii. in the scheme referred to in sec. 80CCD(1) [i.e., NPS]; and
 - iii. in an approved superannuation fund, - to the extent it exceeds ` 7,50,000 in a previous year
- viii. The annual accretion (like interest, dividend, etc.) during the previous year to the balance at the credit of the aforesaid fund or scheme to the extent it relates to the contribution referred above.

Specified Employees [Sec. 17(2)(iii)]

Specified employee means:

1. A director employee.
2. An employee who has substantial interest in the employer company.
3. An employee whose aggregate salary from all employers together exceeds ` 50,000 p.a

Exempted Perquisites

- Tea or snacks
- Food
- Recreational facilities
- Goods sold to employee at concessional rate:
- Conveyance facility
- Training

- Services rendered outside India:
- Contribution in some specified schemes
- Loans.
- Medical facility:
- Periodicals and journals
- Telephone, mobile phones
- Free education facility
- Computer or Laptop
- Movable assets:
- Leave Travel Concession:
- Rent-free accommodation
- Accommodation:
- Tax on non-monetary perquisite paid by employer on behalf of employee.
- Health club, Sports club facility

Valuation of Accommodation

Valuation of Rent-free unfurnished accommodation (RFA) [Rule 3(1)]

- Rent-free accommodation is taxable in the hands of all employees (except the Judges of High Court or Supreme Court and Official of the Parliament or Union Minister and a leader of Opposition).
- a. Central and State Government Employee (including military person): value of perquisite in respect of such accommodation is equal to the licence fee.
- b. Accommodation provided by Government to an employee serving on deputation:
- City Having population exceeding 25 lacs as per 2001 census: Value of perquisite:
 - ✓ 15% of salary for the period during which the employee occupied the said accommodation.
 - ✓ City Having population exceeding 10 lacs but not exceeding 25 lacs as per 2001 census:
 - 10% of salary for the period during which the employee occupied the said accommodation.
 - ✓ Any other city:
 - 7.5% of salary for the period during which the employee occupied the said accommodation.

Salary for the purpose of Rent free Accommodation

- Basic +
- Dearness allowance/pay (if it forms a part of retirement benefit) +
- Bonus +
- Commission +
- Fees +
- All other taxable allowances (only taxable amount) +
- Any other monetary payment by whatever name called

a) Other Employees (residual category)

a. City having population exceeding 25 lacs as per 2001 census

- Accommodation is owned by the employer
 - ✓ 15% of salary for the period during which the employee occupied the said accommodation
- Accommodation is not owned by the employer

Unit 04: Computation of Income under the Head Salaries

- ✓ Rent paid or payable by the employer or 15% of salary, whichever is lower.
- b. Having population exceeding 10 lacs but not exceeding 25 lacs as per 2001 census
 - Accommodation is owned by the employer
 - 10% of salary for the period during which the employee occupied the said accommodation
 - Accommodation is not owned by the employer
 - Rent paid or payable by the employer or 15% of salary, whichever is lower.

Notes

Exemption of 90 days in case of allotment of two houses:

- The value of perquisite shall be taken for only one such house having a lower value for a period not exceeding 90 days.
- Thereafter, the values of both such houses are taxable.

Insurance Premium Payable by Employer

As per sec. 17(2)(v), following sums payable by an employer shall be taxable perquisite in the hands of all employees, whether it is paid directly or through a fund (other than recognised provident fund or approved superannuation fund or deposit-linked insurance fund),

- To effect an assurance on the life of the assessee; or
- To effect a contract for an annuity note: employee can claim deduction u/s 80C for LIC premium paid by employer

Valuation of Sweat Equity Shares Allotted or Transferred to The Assessee

The fair market value of the specified security or sweat equity shares, as the case may be, on the date on which the option is exercised by the assessee	XXXXXXXXXX
Less: The amount actually paid by, or recovered from the assessee in respect of such security or shares	XXXXXXXXXX
Value of perquisite	

Valuation of Perquisites In Respect of Motor Car [RULE 3(2)]

Car is owned by	Employer
Car is Maintained by	Employer
Used by employee for	Office purpose
Taxable value	Not a perquisite
Who is Chargeable	Not chargeable

Car is owned by	Employer
Car is Maintained by	Employer
Used by employee for	Personal purpose
Taxable value	Maintenance cost +Depreciation @ 10% of actual cost of the car.

Income Tax Law and Practice

	However, if the car is not owned by employer then actual hire charge incurred by employer shall be considered.
Who is Chargeable	Specified Employee

Car is owned by	Employer
Car is Maintained by	Employer
Used by employee for	Both official and Personal purpose
Taxable value	. ` 2400 p.m. in case of higher capacity car# and ` 1800 p.m. for lower capacity car.
Who is Chargeable	Specified Employee

Car is owned by	Employer
Car is Maintained by	Employee
Used by employee for	Office purpose
Taxable value	Not a perquisite
Who is Chargeable	Not applicable

Car is owned by	Employer
Car is Maintained by	Employee
Used by employee for	personal purpose
Taxable value	Depreciation @ 10% of actual cost of the car.
Who is Chargeable	Specified employee

Car is owned by	Employer
Car is Maintained by	Employee
Used by employee for	Both purpose
Taxable value	. ` 900 p.m. in case of higher capacity car# and ` 600 p.m. for lower capacity ca
Who is Chargeable	Specified employee

Employee	Employee
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Unit 04: Computation of Income under the Head Salaries

Car is Maintained by	Employer
Used by employee for	Office purpose
Taxable value	Not a perquisite
Who is Chargeable	Not applicable

Employee	Employee
Car is Maintained by	Employer
Personal purpose	Personal purpose
Taxable value	=Maintenance cost
Who is Chargeable	All employee

Employee		Employee
Car is Maintained by		Employee
Personal purpose		Any purpose
Taxable value		Not a perquisite
Who is Chargeable		Not applicable

Valuation of Perquisites In Respect of Free Domestic Servants [RULE 3(3)]

Servant appointed by	Employer
Taxable value of perquisite	Actual cost to the employer is taxable as perquisite
Taxable in hands of	Specified employee

Servant appointed by	Employee
Taxable value of perquisite	Actual cost to the employer is taxable as perquisite
All employee	All employee

Notes:

- a. If rent-free accommodation (owned by the employer) is provided with gardener then gardener's salary and maintenance cost of garden shall not be taxable. [Circular No.122 dated 19/10/1973]
- b. Any amount charged from the employee for such facility shall be reduced from above value.
- c. Domestic servant allowance given to employee is fully taxable.
- d. Reimbursement of servant-salary by the employer shall be taxable in hands of all employee.

Gas, Electricity or Water Facility [RULE 3(4)]

Facility is in name of employee	
Taxable value of perquisite	
Facility Taxable in the hands of is provided from own sources	Manufacturing cost to the employer
Facility is provided from other agency	Prices paid to such agency
Taxable in the hands of	All employees

Facility is in name of employer	
Taxable value of perquisite	
Facility Taxable in the hands of is provided from own sources	Manufacturing cost to the employer
Facility is provided from other agency	Prices paid to such agency
Taxable in the hands of	Specified employees

Valuation of Perquisites In Respect of Free Education [RULE 3(5)]

Facility provided to employee	
Taxable Value	Not taxable

Facility provided to family member	
Facility provided in an institution owned by the employer	Child of the assessee: Cost of such education in similar institution subject to an exemption of ` 1,000 p.m. per child shall be taxable ¹ . Other family member: Cost of such education in similar institution shall be taxable

Facility provided to family member	
Reimbursement of education expenditure to employee.	Actual reimbursement shall be taxable. Such reimbursement of tuition fee shall also be taxable in the hands of Central Government employee. (Circular letter No 35/7/65-IT(B) dt 12/2/1965)
Who is chargeable?	
In case of reimbursement; or School fee of family member of the employee paid by the employer directly to school	All employee
In any other case	Specified employee

Unit 04: Computation of Income under the Head Salaries

Valuation of Perquisites In Respect of Free Transport [RULE 3(6)]

- If employer is engaged in transportation business.
 - ✓ Amount charged from public for such facility is taxable in the hands of specified employee
- In any other case
 - ✓ Actual cost of employer for such facility is taxable in the hands of all employees.

Valuation of Perquisites in Respect of Interest Free Loan or Concessional Rate of Interest [RULE 3(7)(i)]

- Not taxable if aggregate amount of loan given by the employer (or any other person on his behalf) does not exceed ` 20,000.

Valuation of Perquisites In Respect of Free Meals [RULE 3(7)(iii)]

- Tea, snacks or other non-alcoholic beverages in the form of light refreshment provided during office hours (including over-time)
 - ✓ Not taxable

Medical Facility [PROVISO TO SEC. 17(2)]: Medical Facility Provided in India

- Medical facility provided to the employee or his family in a hospital, clinic, dispensary or nursing home maintained by the employer.
 - ✓ Fully Exempted
- Reimbursement of medical bill of the employee or his family of -
 - ✓ Any hospital maintained by Government or Local Authority; or
 - ✓ Any hospital approved by the Government for its employee
 Fully Exempted
- Payment/reimbursement by employer of medical expenses incurred by an employee on himself/his family in a hospital, which is approved by the CCIT, for the prescribed diseases (like Cancer, TB, AIDS, etc.)
 - ✓ Fully Exempted
- Group medical insurance (i.e. Mediclaim) obtained by the employer for his employees.
 - ✓ Fully Exempted
- Any reimbursement by employer of any insurance premium paid by the employee, for insurance of his health or the health of any member of his family.
 - ✓ Fully Exempted

Medical Facility Provided Outside India

- Medical Expenditure
 - ✓ Exempted to the extent permitted by RBI.
- Cost of stay abroad (Patient + One Attendant/Care taker)
 - ✓ Exempted to the extent permitted by RBI. Cost of travel (Patient + One Attendant/Care taker)
 - ✓ Exempted only when gross total Income of the employee excluding this (cost of travel) perquisite, does not exceed ` 2,00,000 p.a.

Summary

Salary is taxable under section 15 on the basis of when it is due or received, whichever occurs first. Any salary owed to an employee from a current or former employer during the previous year would be included in the income subject to income tax under Section 15 regardless of whether it has been paid or not. An employee's basic salary is taxable in their hands. An allowance is described as a certain sum of money given on a regular basis in addition to the employee's wage to

Income Tax Law and Practice

help the employee meet certain obligations related to the service they provided or as payment for exceptional employment conditions. Whether it is paid in addition to the pay or in lieu of it, it is taxable on a due/accrued basis. All perks and extras that an employer provides to an employee in addition to salary and compensation, whether in cash or in kind that may be exchanged for money, are referred to as perquisites. These perks or conveniences may be given freely or as part of a service agreement.

Keywords

Monetary Income means Income chargeable under the salary but excluding perquisite value of all non-monetary perquisites

Wages: Any amount received by a person for work done is called wages. It can also be called as 'Pay', 'Basic Pay', 'Salary', 'Basic salary' or 'Remuneration'.

Gratuity: Any money an employee receives from a former employer as an expression of appreciation for previously provided services is referred to as a gratuity.

Bonuses are payments made to employees over and beyond their regular salaries. Bonuses are completely taxable on a receipt-basis under the heading "Salaries."

Self Assessment

1. Sonam's employer, Vikash Ltd., has given him an automobile (1.7 litres). The cost of the car to the employer was Rs.3.5 million, and Rs.30,000 per year was spent on maintenance. The employer pays the chauffeur a wage of Rs.3,000 per hour. If the car is utilised for: Office purposes, find the value of the Sonam perquisite for the years A.Y.2022-23.
 - A. Nil
 - B. 15,000
 - C. 86,000
 - D. 39,600

2. Sonam's employer, Vikash Ltd., has given him an automobile (1.7 litres). The cost of the car to the employer was Rs.3.5 million, and Rs.30,000 per year was spent on maintenance. The employer pays the chauffeur a wage of Rs.3,000 per hour. If the car is utilised for: personal purposes, find the value of the Sonam perquisite for the years A.Y.2022-23. Employees are charged Rs. 15,000 per year for these facilities.
 - A. Nil
 - B. 15,000
 - C. 86,000
 - D. 39,600

3. Sonam's employer, Vikash Ltd., has given him an automobile (1.7 litres). The cost of the car to the employer was Rs.3.5 million, and Rs.30,000 per year was spent on maintenance. The employer pays the chauffeur a wage of Rs.3,000 per hour. If the car is utilised for: both office and personal purposes, find the value of the Sonam perquisite for the years A.Y.2022-23. Employees are charged Rs. 15,000 per year for these facilities.
 - A. Nil
 - B. 15,000
 - C. 86,000
 - D. 39,600

4. Standard Deduction [Section 16(ia)] is:

Unit 04: Computation of Income under the Head Salaries

- A. 25000
B. 40,000
C. 50,000
D. 1,00,000
5. Entertainment Allowance [Section 16(ii)] which monetary limit is used to determine deduction?
A. 5000
B. 40,000
C. 50,000
D. 1,00,000
6. Entertainment Allowance [Section 16(ii)] what percentage of basic salary is used to determine deduction?
A. 10
B. 20
C. 30
D. 40
7. If the Car is owned / hired by the employer; expenses met by the employer & is used by the employee partly for Official and partly for Personal purposes, the taxable value of the perquisite if the cc of the engine is Up to 1.6 litres, as under(pm):
A. 1200
B. 1800
C. 2100
D. 2500
8. If the Car is owned / hired by the employer; expenses met by the employer & is used by the employee partly for Official and partly for Personal purposes, the taxable value of the perquisite if the cc of the engine is >1.6 litres, as under(pm):
A. 1200
B. 1800
C. 2400
D. 2500
9. If the Car is owned / hired by the employer; expenses met by the employer & is used by the employee partly for Official and partly for Personal purposes, the taxable value of the perquisite would be based on the cc of the engine and if chauffeur is also provided, INR pm is to be added to either of the above, depending on the engine capacity.
A. 900
B. 1800
C. 2400
D. 2500
10. If the Car is owned / hired by the employer; expenses met by the employer & is used by the employee partly for Official and partly for Personal purposes, the taxable value of the perquisite would be based on the cc of the engine(Up to 1.6 litres), as underpm:

- A. 900
B. 600
C. 2400
D. 2500
11. If the Car is owned / hired by the employer; expenses met by the employee & is used by the employee partly for Official and partly for Personal purposes, the taxable value of the perquisite would be based on the cc of the engine (> 1.6 litres), as under pm:
A. 900
B. 600
C. 2400
D. 2500
12. if the educational institution is owned by the employer, and free educational facilities are provided to the employee's children, there wouldn't be any perquisite as long as the value of benefit in a month is < INR
A. 900
B. 1000
C. 2400
D. 2500
13. in case of Use of movable assets by employee / any member of his household, value of perquisite is: p.a. of the actual cost of the asset, if it is owned by the employer OR the actual hire charges incurred by the employer if the asset is hired as reduced by the amount, if any, paid or recovered from the employee for such use would be the taxable value of the perquisite
A. 10
B. 20
C. 30
D. 40
14. Where the accommodation is provided by the employer in a hotel (except where the employee is provided such accommodation for a period not exceeding in aggregate 15 days on the transfer from one place to another): The perquisites value would be % of salary paid.
A. 10
B. 24
C. 30
D. 40
15. For a furnished accommodation,% p.a. of the furniture cost is added to the value obtained above for unfurnished.
A. 10
B. 24
C. 30
D. 40

Unit 04: Computation of Income under the Head Salaries**Answers for Self Assessment**

- | | | | | |
|-------|-------|-------|-------|-------|
| 1. A | 2. C | 3. D | 4. C | 5. A |
| 6. B | 7. B | 8. C | 9. A | 10. B |
| 11. A | 12. B | 13. A | 14. B | 15. A |

Review Questions

1. Write a short note on Medical Facility Provided Outside India
2. Distinguish between House Rent Allowance and Rent Free Accommodation.
3. Distinguish between Allowances and Perquisites.
4. Write a note on Profit in lieu of salary.
5. Write a note on Entertainment Allowance.

**Further Readings**

- https://www.icsi.edu/media/webmodules/16112021_Advance_Tax_Laws.pdf
- Income Tax Law & Practice A.Y 2021-22 by Dr H.C. Mehrotra and Dr. S. P. Goyal. Sahitya Bhawan Publications
- Study Material on Direct Tax Laws and International Taxation by ICAI
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Unit 05: Computation of Income under the Head House Property

CONTENTS

Objectives

Introduction

- 5.1 Chargeability [SEC. 22]
- 5.2 Provision for arrears of rent and unrealized rent received subsequently [section 25a]
- 5.3 Taxes Levied by Local Authority (Municipal Tax) [Proviso to SEC. 23(1)]
- 5.4 Self-Occupied Property [SEC. 23(2)(a)]
- 5.5 Deemed to Be Let-Out House Property [SEC. 23(4)]
- 5.6 Determination of Annual Value for Different Types of House Properties

Summary

Keywords

Self Assessment

Answers for Self Assessment

Review Questions

Further Readings

Objectives

After studying this unit, you will be able to:

- appreciate the meaning of the important terms Under the head house property.
- determine annual value of different categories of house property;
- Compute income from house property for different categories of house property

Introduction

Sections 22 to 27 of the Income Tax Act of 1961 deal with the provisions for calculating income from house property. The charging part of the Act, Section 22, outlines the basis of charge, with the annual value being specified as the foundation for calculating Income from House Property. The process of computation of "Income from House Property" starts with the determination of annual value of the property. The concept of annual value and the method of determination are laid down in section 23. The admissible deductions available from house property are mentioned in section 24. The coverage of the lesson would include the computation of income under the head of House Property. the prerequisites that must be met for revenue to be charged under this heading. How to calculate the yearly value of various types of residential properties, acceptable and unacceptable deductions from annual value, the tax treatment of unrealized rent, who is considered an owner, what co-ownership entails, how co-ownership is treated tax-wise, etc.

5.1 Chargeability [SEC. 22]

Three criteria

- House Property
- Owner
- Not used in Business or Profession

The term House Property

- any land surrounded by walls having a roof or not; and any land appurtenant to a building.

Owner

Owner includes

- legal owner,
- beneficial owner and
- deemed owner.

Fictional owner or Deemed owner [Sec. 27]

- Transfer to spouse or minor child [Sec. 27(i)];
- The holder of an impartible estate [Sec. 27(ii)]
- Property held by a member of a company, society or any other association [Sec. 27(iii)];
- A person who acquired a property u/s 53A of the Transfer of Property Act [Sec. 27(iiiia)];
- Lessee of a building u/s 269UA(f) [Sec. 27(iiiib)];

Foreign property

- Ordinarily resident: Always taxable
- Not ordinarily resident or Non resident Income: must be received in India

Disputed ownership

- Person who is in receipt of an income or who enjoys the possession of the property is assessable to tax

Composite rent

- Composite Rent = Rent for building + Rent for assets / Charges for various services

Co-ownership [Sec. 26]

- If two or more persons own a house property jointly, then they are known as co-owners.
- Tax treatment
- Share of each co-owner in the income from the property as computed in accordance with sec. 22 to 25 shall be included in his total income.
- Where the house property is owned by co-owners and is occupied by each of the co-owner then all of them can claim benefit u/s 23(2)(a) and interest on loan shall be allowed to all the co-owners to an extent of ` 30,000/` 2,00,000 as the case may be. Note: Provision of Sec. 26 is mandatory and not optional

EXEMPTED PROPERTIES

1. Any one palace or part there of an ex-ruler, provided the same is not let out [Sec. 10(19A)].
Tax-point: If the ex-ruler has a house property and the part of which is self-occupied and remaining is let out then only the self-occupied part of the house property shall be exempted.
2. House property of a local authority [Sec. 10(20)].
3. House property of an approved scientific research association [Sec. 10(21)].
4. House property of an educational institution [Sec. 10(23C)].
5. House property of a hospital [Sec. 10(23C)].
6. House property of a person being resident of Ladakh [Sec. 10(26A)]
7. House property of a political party [Sec. 13A]
8. House property of a trade union [Sec. 10(24)]
9. A farm house [Sec. 10(1)]
10. House property held for charitable purposes [Sec. 11]

11. House property used for own business or profession [Sec. 22]

Property held as stock-in-trade [Sec. 23(5)]

- Up to 2 year from the end of the financial year in which the certificate of completion of the construction of a property is obtained from the competent authority: Annual value to be nil
- After the completion of aforesaid period: Annual value is computed as per other provisions

Doctrine of mutuality

- The case of a club,
- providing recreational facilities exclusively to its members and the guests
- the annual value of the club house shall be exempted from tax

Gross Annual Value (GAV)

- Earning capacity is termed as Annual Value

Actual Rent Receivable [ARR]

- Any sum receivable as rent of the house property for the previous year is an evidence for determining the earning capacity of the building.
- Computed on accrual basis.

Any sum receivable as rent of the house property for the previous year is an evidence for determining the earning capacity of the building. Such actual rent receivable is to be computed on accrual basis. However, where tenant pays rent, which is influenced by benefits provided by the owner of the property, such rent must be disintegrated to determine actual rent i.e. De-facto rent of the property. De facto rent = ARR – Cost of amenities. Tax point: While computing actual rent receivable, outstanding rent shall be considered but an advance rent received during the financial year is not to be considered

Gross Municipal Value

- It means the annual value of the property decided by the municipality on which they charge municipal tax.
 - Such valuation may also be taken as an evidence for earning capacity of a property.
 - In metro cities (i.e. Chennai, Delhi, Kolkata, Mumbai), municipal authorities charge tax on Net Municipal Value after giving a deduction for repairs (being 10% of Gross Municipal value) and an allowance for service taxes (like sewerage tax, water tax etc. as a % of Net Municipal value).
 - Hence, the relation between Gross Municipal Value and Net Municipal Value can be concluded as under

Fair or Notional rent of the property

- Fair or notional rent of a property means rent fetched by a similar property in a similar or the same locality
 - Though two properties might not be exactly similar still it is an indicator of rent reasonably expected from the property.
 - An inflated or deflated rent due to an emergency, relationship and such other conditions need to be adjusted to determine fair rent.
 - For instance, a property was let out to a friend for a monthly rent of ₹ 2,000 which might
 - be let out to another person at the rate of ₹ 2,500 p.m. In such case, fair rent of the property shall be ₹ 2,500 p.m

Standard rent under the Rent Control Act

- Standard rent is the maximum rent, which a person can legally recover from his tenant under the Rent Control Act

Expected Rent (ER)

- The Expected Rent (ER) is the higher of the fair rent (FR) and municipal value (MV), but restricted to standard rent (SR).

Unrealised Rent [Rule 4]

- The tenancy is bona fide; Direct Taxation 130 The Institute of Cost Accountants of India
- The defaulting tenant has vacated the property or steps have been taken to compel him to vacate the property;
- The defaulting tenant is not in an occupation of any other property of the assessee;
- The assessee has taken all reasonable steps to institute legal proceeding for the recovery of the unpaid rent or has satisfied the Assessing Officer that legal proceedings would be worthless

5.2 Provision for arrears of rent and unrealized rent received subsequently [section 25a]

- Taxable in the year of receipt/ realization
- Deduction@30% of rent received/ realized
- Taxable even if assessee is not the owner of the property in the financial year of receipt/ realization
- As per section 25A (1), the amount of rent received in arrears from a tenant or the amount of unrealized rent realized subsequently from a tenant by an assessee shall be deemed to be an income from house property in the financial year in which such rent is received or realised, and shall be included in the total income of the assessee under the head "Income from house property", whether the assessee is the owner of the property or not in that financial year.
- Section 25A (2) provides a deduction of 30% of arrears of rent or unrealised rent realised subsequently by the assessee

5.3 Taxes Levied by Local Authority (Municipal Tax) [Proviso to SEC. 23(1)]

- Tax levied by the municipality or local authority is deductible from Gross Annual Value (GAV).
- Computed as a % of Net Municipal Value
- Allowed as deduction subject to the following conditions:
 - Actually paid during the previous year.
 - Paid by the assessee.
 - Related to the previous year or any year preceding the previous year
- Tax levied by the municipality or local authority is deductible from Gross Annual Value (GAV).
- As per sec. 27(vi), taxes levied by a local authority in respect of any property shall include service taxes levied by local authority in respect of such property.

5.4 Self-Occupied Property [SEC. 23(2)(a)]

- As per sec. 23(2)(a), a house property shall be termed as self-occupied property where such property or part thereof:
- is in the occupation of the owner for the purposes of his own residence;
- is not actually let out during the whole or any part of the previous year; and
- no other benefit is derived by the owner

Types of Self Occupied houses

- Fully self-occupied
- Partly self-occupied & partly vacant
- Partly self-occupied & partly let out
- Partly self-occupied & partly use for business purpose

Unoccupied Property [SEC. 23(2)(b)]

- Not occupied by the owner owing to his employment, business or profession carried on at any other place and hence he has to reside at that place in a building not belonging to him, such house shall be termed as unoccupied property.
- Where an assessee has a residential house (kept for self-occupation)
- and it cannot actually be occupied by the owner owing to his employment, business or profession carried on at any other place and
- hence he has to reside at that place in a building not belonging to him, such house shall be termed as unoccupied property. Tax point:

5.5 Deemed to Be Let-Out House Property [SEC. 23(4)]

- Where the assessee occupies more than two house properties as self-occupied or
- has more than two unoccupied properties,
- then for any two of them, benefit u/s 23(2) can be claimed (at the choice of the assessee) and remaining property or properties shall be treated as 'deemed to be let out'.

5.6 Determination of Annual Value for Different Types of House Properties

- Where the property is let out throughout the previous year [Section 23(1)(a)/(b)]
- Where let out property is vacant for part of the year [Section 23(1)(c)]
- In case of self-occupied property or unoccupied property [Section 23(2)]
- Where a house property is let-out for part of the year and self-occupied for part of the year [Section 23(3)]
- In case of deemed to be let out property [Section 23(4)]
- In case of a house property held as stock-in-trade [Section 23(5)]

Where the property is let out throughout the previous year [Section 23(1)(a)/(b)]

GAV:

- higher of -
 - a. Expected Rent (ER) and
 - b. Actual rent received or receivable during the year

NAV:

- GAV-municipal taxes paid by the owner

Illustration 1

Particulars	House I	House II	House III	House IV	House V
	()	()	()	()	()
Municipal Value	1,60,000	1,10,000	1,30,000	48,000	1,60,000
Fair Rent	1,80,000	1,20,000	1,30,000	50,000	1,50,000
Standard Rent	NA	1,50,000	1,16,000	NA	1,56,000
Actual rent received/receivable	1,44,000	1,44,000	1,20,000	60,000	1,44,000

Particulars	House I	House II	House III	House IV	House V
	()	()	()	()	()
Municipal value(i)	160000	110000	130000	48000	160000
Fair rent(ii)	180000	120000	130000	50000	150000
Higher of (i) & (ii)	180000	120000	130000	50000	160000
(iii) Higher of (i) & (ii)	180000	120000	130000	50000	160000
Standard rent(iv)	NA	150000	116000	NA	156000
Expected rent [Lower of (iii) & (iv)]	180000	120000	116000	50000	156000
Actual rent received/receivable	144000	144000	120000	60000	144000
GAV [Higher of ER & AR]	180000	144000	120000	60000	156000

Computation of “income from house property” for property let out throughout the previous year

- GAV Computation
- Step 1 Compute ER: Higher of MV and FR, but restricted to SR
- Step 2 Compute Actual rent received/receivable Less UR
- Step 3 Comparison of ER and Actual rent received/receivable
- Step 4 GAV is the higher of ER and Actual rent received/receivable

Income from house property

Gross Annual Value (GAV)(A)

Less: Municipal taxes (paid by the owner during the previous year)(B)

Net Annual Value (NAV) = (A-B)

Less: Deductions u/s 24

(a) 30% of NAV D

(b) Interest on borrowed capital (actual without any ceiling limit)

Income from house property

Where let out property is vacant for part of the year [Section 23(1)(c)]

- GAV= actual rent received or receivable

In case of self-occupied property or unoccupied property [Section 23(2)]

- Annual Value will be Nil.
- The benefit of “Nil” Annual Value is available only for upto two self-occupied or unoccupied house properties. Available only to an individual/ HUF.
- No deduction for municipal taxes

Computation of Taxable Income of Self-Occupied Property

- Net Annual Value Nil
- Less: Interest on borrowed capital u/s 24(b) Income from house property
- Standard deduction u/s 24(a) is not available

Net Annual value of two self-occupied house properties, at the choice of the assessee, is taken as nil.

He can choose those house properties as self-occupied through which tax liability can be reduced.

Normally (but not always) house property with higher gross annual value is treated as self-occupied property but it is advised to calculate total income under the head ‘Income from house property’ by applying each option separately and then choose the option which reduces total income.

Illustration 2

	I	II	III
SR	3,00,000	30,00,000	36,00,000
MV	4,00,000	26,00,000	27,00,000
Fair rent	5,00,000	32,00,000	38,00,000
Municipal tax (10% of municipal value) paid			
Interest on loan taken for purchases of houses	1,80,000	3,40,000	3,30,000

Solution:

1. House I deemed to be let out

MV	4,00,000
Fair rent	5,00,000

Income Tax Law and Practice

MV or FRV whichever is higher	5,00,000
SR	3,00,000
ER	3,00,000

NAV

ER	3,00,000
Less Municipal tax (10% of municipal value) paid	40,000
NAV	2,60,000

Income from Let out House Property

NAV	2,60,000
Deduction	
SD 30% of NAV	78,000
Interest on loan taken for purchases of houses	1,80,000
Deductions	2,58,000
Income from Let out House Property	2,000

2. House II and III-Self Occupied

NAV= NIL

Less = (2,00,000)

(24(b) Interest on loan [(3,40,000 + 3,30,000), subject to max. of 2,00,000])

Income from Self Occupied House Property= (2,00,000)

Income from House property

- Income from Let out House property: 2000
- Income from Self Occupied House
- Property= (2,00,000) Income from House property
(1,98,000)

Where a house property is let-out for part of the year and self-occupied for part of the year [Section 23(3)]

- ER for the whole year shall be taken into account for determining the GAV.
- The ER for the whole year shall be compared with the **actual rent for the let out period** and whichever is higher shall be adopted as the GAV.
- Deduction for municipal tax for the whole year.

Illustration 3

- House property for self-occupation for 4 months
- let out for 8 months for rent of 12,000 p.m. Municipal value 2,00,000
- Fair Rent = 1,60,000
- Standard Rent= 1,92,000

- Municipal tax =10%
- Interest on loan = 20,000

Solution

- Municipal value 2,00,000
- Fair Rent = 1,60,000
- Standard Rent= 1,92,000
- ER= 192000
- (Higher of MV & FR (RER cannot exceed SR))
- ER= 1,92000
- AR=12000*8=96000
- Gross Annual Value = 192000
- (Higher of RER and ARR)
- GAV= 192000
 - Less M. Tax= 20,000
 - (10% of MRV=10% of 2,00,000=20,000)
- NAV= 172000
 - Less: deduction u/s 24 SD= 51600 (30% of 172000)
- Interest on loan=20,000
- Income from house property=100400

In case of deemed to be let out property [Section 23(4)]

- More than 2 properties for self-Occupation:
- Annual Value of any 2 properties taken to be NIL.
- Other self-occupied/unoccupied properties shall be treated as “deemed let out properties.

Illustration4: Three houses self-occupied

Particulars	House I	House II	House III
Municipal valuation p.a.	6,00,000	7,20,000	6,60,000
Fair rent p.a.	7,50,000	5,50,000	7,60,000
Standard rent p.a.	7,00,000	7,40,000	7,50,000
Date of completion/purchase	31.3.1999	31.3.2002	01.4.2015
Municipal taxes paid during the year	10%	8%	6%
Interest on money borrowed for repair of property during the current year		1,10,000	0
Interest for current year on money borrowed in April, 2015 for purchase of property	0	0	3,50,000

Solution

Income Tax Law and Practice

Particulars		Amount in		
		House I	House II	House III
Gross Annual Value (GAV)				
ER is the GAV of house property		700000	720000	750000
Less:	Municipal taxes (paid by the owner during the previous year)	60,000	57,600	39,600
Net Annual Value (NAV)		6,40,000	6,62,400	7,10,400
Less:	Deductions under section 24			
	(a) 30% of NAV	1,92,000	1,98,720	2,13,120
	(b) Interest on borrowed capital	-	1,10,000	3,50,000
Income from house property		4,48,000	3,53,680	1,47,280

Option 1: House III deemed to be let out

Particulars	Amount in
House I (Self-occupied)	Nil
House II (Self-occupied) (interest deduction restricted to 30,000)	-30,000
House III (Deemed to be let-out)	1,47,280
Income from house property	1,17,280

OPTION 2 (House II - deemed to be let out)

Particulars	Amount in `
House I (Self-occupied)	Nil
House II (Deemed to be let-out)	3,53,680
House III (Self-occupied)	(2,00,000)
Income from house property	153680

OPTION 3 (House I - deemed to be let out)

Particulars	Amount in
House I (Deemed to be let-out)	4,48,000
House II (Self-occupied) (interest deduction restricted to 30,000)	-30,000

House III (Self-occupied)	-3,50,000	
(Total interest deduction restricted to 2,00,000)		-2,00,000
Income from house property		2,48,000

In case of a house property, a portion let out and a portion self-occupied

- Separate treatment for Let-out and Self-Occupied part.
- Whole property not treated as a single unit.
- Municipal valuation/fair rent/standard rent, if not given separately, shall be apportioned between the let-out portion and self-occupied portion.
- Property taxes, if given on a consolidated basis, can be bifurcated.

Illustration 5

- A house property with two separate residential units:
- unit A covers 40% of the total area(self-occupied)
- Unit B covers 60% of the total area (let out for a monthly rent of 6,000).

MV	200000
FRV	2,40,000
SR	400000
M. Tax	10%
Interest on Loan	60000
Annual repair charge	10,000

Solution: GAV

Particulars	Unit A	Unit B
MV	80000	120000
FRV	96000	144000
SR	160000	240000
ER	NIL	144000
Actual Rent(6000*12)		72000
GAV		144000

Solution:Computation of Income from house property

Particulars	Unit A	Unit B
Gross Annual Value		144000

Income Tax Law and Practice

Less. M Tax 10% of 120000		12000
NAV		132000
Less Deductions U/s 24		
SD 30% of NAV 30% *132000		39600
Interest on Loan	24000	36000
Income from house property	(24000)	3600
Income under the head 'Income from house property' -24000+3600	(20400)	

Illustration 6

- The house property has two equal dimension residential units.
- Unit 1 :self-occupied
- unit 2: let out for 9 months for 20,000 p.m.

MV	2,00,000
FRV	1,60,000
SR	3,00,000
M. Tax 10%(70% paid by assessee)	
Interest on loan	80,000
Expenditure on repairs	40,000

Solution

MV	2,00,000	2,00,000
FRV	1,60,000	1,60,000
Mv or FRV whichever is higher	2,00,000	2,00,000
SR	3,00,000	3,00,000
ER(ER cannot exceed SR)	Nil	2,00,000

GAV

ER(ER cannot exceed SR)	Nil	2,00,000
Actual rent Receivable	20000*9	1,80,000
Gross Annual Value		2,00,000

NAV

Gross Annual Value		2,00,000
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Less M. Tax		14,000
NAV		1,86,000
Less: Deduction u/s		
24(a) Standard Deduction		-55800
24(b) Interest on loan	-40000	-40000
Income from house property	-40000	-90200

Recovery of unrealized rent and arrears rent [sec. 25a]

House property let out since 1/4/2017 for monthly rent of 20,000.

On 1/4/2021, as per court decision rent was increased to 24,000 p.m. with retrospective effect from 1/4/2019 and duly paid by in the same year.

Legal expenditure for such suit has been incurred 50,000.

Solution

- Arrears rent belongs to the period 1/4/2019 to 31/3/2021 for 24 months.
- Arrears rent received = 4,000 * 24 months = 96,000
- Taxable in the year of receipt.

Arrears of rent received 96,000

- Less: Standard deduction u/s 24(a) equal to 30% of such rent 28,800
- Income from house property u/s 25A 67200

Summary

According to Section 22 of the Act, "the annual value of property consisting of any buildings or lands appurtenant thereto of which the assessee is the owner, other than such portions of such property which he may occupy for the purposes of any business or profession carried on by him, the profits of which are chargeable to income-tax, shall be chargeable to income-tax under the head Income from House Property." The annual value of the property, or the innate ability of a building to generate income, serves as the yardstick for assessing income tax under this heading. The Income-tax Act's Section 23(1) provides a definition of the term "annual value". After taking into account the standard deduction, which is equivalent to 30% of the annual value, and interest on borrowed capital, income taxable under the heading "Income from House Property" as of Assessment Year 2002-03 will be calculated.

Keywords

*Building means a permanent structure made of bricks, stones, concrete etc. and which has a foundation, walls and doors. It does not include temporary structures.

Composite rent means the rent charged not only for the property to be let out but also for the other facilities like furniture, Lift, Security, Power Back-up etc

Municipal tax includes services related tax like Water tax and Sewerage Tax levied by any local authority in respect of any house property to the extent to which such taxes are borne and paid by the owner, and include enhanced municipal tax finally determined on appeal and payable by assessee

STANDARD DEDUCTION U/S 24(a) is Deduction @ 30% flat deduction on the Net Annual Value. This deduction is allowed even if no expenditure is incurred by the assessee.

Income Tax Law and Practice

A self-occupied property means a property owned by the taxpayer which is occupied throughout the year by the owner for the purposes of his own residence and is not actually let out during the whole or any part of the year.

Self Assessment

1. Under the heading "Income from House Property," tax is due on rental income from a building or land accessory to it that belongs to thetaxpayer.
 - A. Owner
 - B. Power of attorney holder
 - C. Sub-tenant
 - D. Holder in due course

2. Rental income received by a tenant from sub-letting is also charged to tax under the head
 - A. Income from House Property.
 - B. Income from other sources
 - C. Income from business
 - D. Income from Salary

3. The _____ shall be assumed to be the owner of the property if an individual transfers his or her home without due consideration to either his or her spouse (not being a transfer in connection with an agreement to live apart) or to his or her minor kid (not being married daughter).Transferor
 - A. Transferee
 - B. Transferor:
 - C. Transferor: 60% and transferee: 40%
 - D. Transferor: 40% and transferee: 60%

4. In a case where letting out of building and letting out of other assets are inseparable, entire rent (i.e. composite rent) will be charged to tax under the head;
 - A. Income from House Property.
 - B. Income from businessand profession or Income from other sources
 - C. Capital gains
 - D. Income from Salary

5. In a case where, letting out of building and letting out of other assets are separable, rent of building will be charged to tax under the head charged to tax under the head _____.
 - A. Income from House Property
 - B. Profits and gains of business and profession
 - C. Income from other sources
 - D. Capital Gains

6. In a case where, letting out of building and letting out of other assets are separable, rent of other assets will be charged to tax under the head _____.
 - A. Income from House Property
 - B. Profits and gains of business and profession or Income from other sources as the case may be
 - C. Income from Salary
 - D. Capital Gains

7. Deduction available under section 24(a) is _____% of NAV.
- A. 10
 - B. 30
 - C. 50
 - D. 70
8. In case of a property covered under the Rent Control Act, reasonable expected rent will be _____municipal value or fair rent subject to standard rent of the property.
- A. Lower of
 - B. Equal to
 - C. Higher of
 - D. Average of
9. Deduction under section 24(b) is available on account of _____
- A. Municipal taxes paid by the owner
 - B. Capital expenditure incurred by the owner
 - C. Revenue expenditure incurred by the owner
 - D. Interest on capital borrowed for the purpose of purchase, construction, repair, renewal or reconstruction of the property
10. Which of the following treatments is wrong?
- A. If a person occupies more than two properties for his residence, then the SOP benefit will be granted in respect of all such properties occupied by him for his residence.
 - B. If a person occupies more than two properties for his residence, then the SOP benefit will be granted only in respect of any two properties as selected by him
 - C. If a person occupies more than two properties for his residence, then the SOP benefit will be granted only in respect of any two properties as selected by him and other property/properties will be treated as "Deemed to be let-out".
 - D. If a person occupies more than two properties for his residence, the properties not getting SOP benefit are will be treated as "Deemed to be let-out".
11. Which of the following treatments is wrong in regard to Computation of income when, part of the property is self-occupied and part is let out?
- A. A house property may consist of two or more independent units, one of which is self-occupied and the remaining is/are used for any other purpose (i.e., let-out or used for own business).
 - B. A Part/unit which is occupied by the taxpayer for his residence throughout the year will be treated as an independent property and income from such a part/unit will be computed in the manner as discussed in case of a self-occupied property.
 - C. A Part/unit which is let out will be treated as an independent property and income from such a part/unit will be computed in the manner as in case of let out property.
 - D. A Part/unit which is let out will be treated as an independent property and income from such a part/unit will be computed in the manner as in case of self-occupied property.
12. In Tax treatment of unrealizedrent which is subsequently realized, amount received is charged to tax after deducting a sum equal to% of such unrealized rent.
- A. 10

- B. 30
- C. 50
- D. 70

13. In Tax treatment of arrears of rent which is subsequently realized, amount received is charged to tax after deducting a sum equal to% of such unrealized rent.

- A. 10
- B. 30
- C. 50
- D. 70

14. As per Section 80EE of the Income-tax Act, deduction of up to Rs.is allowed to an Individual towards interest on loan taken for acquisition of a residential house property.

- A. 50,000
- B. 60,000
- C. 70,000
- D. 80,000

15. As per Section 80EE of the Income-tax Act, deduction is allowed to an Individual towards interest on loan taken for acquisition of a residential house property provided the amount of loan should not exceed Rs. lakhs.

- A. 25
- B. 35
- C. 45
- D. 55

Answers for Self Assessment

- | | | | | |
|-------|-------|-------|-------|-------|
| 1. A | 2. B | 3. B | 4. B | 5. A |
| 6. B | 7. B | 8. C | 9. D | 10. A |
| 11. D | 12. B | 13. F | 14. A | 15. B |

Review Questions

1. What is the meaning of 'Owner of House Property' under Section 27 of the Income-tax Act, 1961?
2. What is 'annual value' of house property? How is it computed?
3. In computing the income from house property what deductions are allowed from the net annual value?
4. What is the basis of computation of income from House property?
5. How would you arrive at the net annual value of a house occupied by an assessee for his own residence?
6. How would you deal with the Vacancy Allowance while calculating the income under 'Income from house property'?



Further Readings

- https://www.icsi.edu/media/webmodules/16112021_Advance_Tax_Laws.pdf
- Income Tax Law & Practice A.Y 2021-22 by Dr H.C. Mehrotra and Dr. S. P. Goyal. Sahitya Bhawan Publications
- Study Material on Direct Tax Laws and International Taxation by ICAI
- Direct Tax Laws and Practice by Dr. Girish Ahuja & Dr. Ravi Gupta
- <https://incometaxindia.gov.in/tutorials/12.%20income-from-house-property.pdf>

Unit 06: Computation of Income under the Head Capital Gains**CONTENTS**

Objectives

Introduction

6.1 Capital Asset [Sec. 2(14)] Amended

6.2 Types of Capital Asset

6.3 Capital gains

6.4 Period of Holding

6.5 Basis of Charge

6.6 Transfer: What It Means? [Section 2(47)]

6.7 Transactions Not Regarded as Transfer (Sec. 46 & 47) Amended

6.8 Computation of Capital Gains [SEC. 48]

6.9 Exemptions u/s 54

Summary

Keywords

Self Assessment

Answers for Self Assessment

Review Questions

Further Readings

Objectives

After studying this unit, you will be able to:

- Comprehend and identify the assets classified as “capital assets” for the purposes of chargeability under this head;
- Comprehend the meaning of short-term capital asset and long-term capital asset;
- Compute the period of holding for determining whether an asset is a short-term capital asset or long-term capital asset;
- Comprehend the basis of charge under this head;
- Identify the transactions to be considered as transfer for the purpose of capital gains
- Identify the transactions not regarded as transfer;

Introduction

Any profit or gain realized through the sale of a "capital asset" is referred to as a "capital gain." To be eligible for taxes during the current year, the transfer of such a capital asset should have been completed in the prior fiscal year. The entire sale's value is subject to taxation under the income category known as "Capital Gain." It is necessary to pay taxes on the income earned since the profit from the sale falls under the heading of "income." There are two sorts of capital gains: short-term capital gains tax (STCG) and long-term capital gains tax. The tax paid is referred to as capital gains tax (LTCG). The benefit of indexation is not available to LTCG on stocks or equity mutual funds. According to your slab rate, STCG is assessed. The holding time for determining whether a tax is LTCG or STCG varies depending on the asset.

6.1 Capital Asset [Sec. 2(14)] Amended

- Any kind of property held by an assessed, whether or not in connection with his business or profession;
- Any securities held by a Foreign Institutional Investor which has invested in such securities in accordance with the regulations made under the Securities and Exchange Board of India Act, 1992;
- Any unit linked insurance policy to which exemption u/s 10(10D) does not apply due to applicability of the fourth and fifth provisos thereof¹

Capital asset does not include

- (1) Stock in trade
- (2) Personal effect
- (3) Agricultural land in rural area
- (4) Gold Bonds
- (5) Special Bearer Bond
- (6) Gold Deposit Bonds

Agricultural land in rural area Agricultural land in India is not a capital asset except the following

- Land which is situated within the jurisdiction of any Municipality (whether known as a municipality, municipal corporation, notified area committee, town area committee, town committee, or by any other name) or Cantonment Board having population of 10,000 or more; or
- In any area within the distance, measured **aerially**, –

Population of the municipality or cantonment board	Area within the aerial distance from the local limits of such municipality or cantonment board is non-rural area
More than 10,000 but not exceeding 1,00,000	Upto 2 kilometres
More than 1,00,000 but not exceeding 10,00,000	Upto 6 kilometres
More than 10,00,000	Upto 8 kilometres

6.2 Types of Capital Asset

Short Term Capital Asset [Sec. 2(42A)]

Long Term Capital Asset [Sec. 2(29A)]

Short Term Capital Asset [Sec. 2(42A)]

- It means a capital held by an assessee for not more than 36 months immediately before the date of transfer.

Long Term Capital Asset [Sec. 2(29A)]

- A capital asset, which is not a short-term capital asset, is a long-term capital asset.

Exceptions:

Short-term capital asset (STCA) if it is held for not more than 12 months before the date of transfer:

- Equity or preference share in a company (listed in India)

Unit 06: Computation of Income under the Head Capital Gains

- Any security e.g. debenture, Government securities, etc. (listed in India)
- A unit of an equity oriented fund¹ (whether quoted or not)
- Zero-Coupon Bonds (whether quoted or not) • Units of UTI (whether quoted or not)
- Short-term capital asset (STCA) if it is held for not more than 24 months before the date of transfer:
- Equity or preference share in an unlisted company
- Immovable property being land or building or both

6.3 Capital gains

- Short-term capital gain (STCG)
 - Arises on transfer of short-term capital assets (STCA)
- Long-term capital gain (LTCG)
 - Arises on transfer of long-term capital assets (LTCA).

6.4 Period of Holding

In determining period of holding of any capital asset by the assessee in the circumstances stated below, the period shall be determined by considering the period specified as against them:

1. Where shares held in a company in liquidation:
The period subsequent to the date of liquidation of company shall be excluded.
2. Where asset becomes the property of an assessee by virtue of section 49(1)
The period for which the capital asset was held by the previous owner shall be included.
3. Where inventory of business is converted into or treated as a capital asset by the assessee
Period from the date of conversion or treatment as a capital asset shall be considered
4. Where share/s in the Indian company (amalgamated company), becomes the property of an assessee in lieu of share/s held by him in the amalgamating company at the time of transfer referred under section 47(vii).
The period for which the share(s) was held by the assessee in the amalgamating company shall be included
5. Where the share or any other security is subscribed by the assessee on the basis of right to subscribe to any share or security or by the person in whose favor such right is renounced by the assessee
Period from the date of allotment of such share or security shall be reckoned
6. Where the right to subscribe to any share or security is renounced in favour of any other person
Period from the date of offer of such right by the company or institution shall be reckoned.
7. Where any financial asset is allotted without any payment and on the basis of holding of any other financial asset.
Period from the date of allotment of such financial asset shall be reckoned.
8. Where share/s in the Indian company being a resulting company becomes the property of an assessee in consideration of demerger.
The period for which the share/s were held by the assessee in demerged company shall be included.

Income Tax Law and Practice

9. Where equity share in a company becomes the property of the assessee by way of conversion of preference shares into equity shares referred under section 47(xb)

The period for which the preference shares were held by the assessee shall be included.

10. Where any specified security or sweat equity shares is allotted or transferred, directly or indirectly, by the employer free of cost or at concessional rate to his employees (including former employees).

Period from the date of allotment or transfer of such specified security or sweat equity shares shall be reckoned.

11. Period of holding in respect of other capital assets

- CBDT Rules

Illustration 1

- How will the period of holding be determined in the case of the following assets?
 1. Shares held in a company in liquidation
 2. Bonus shares
 3. Flat in a co-operative society

Solution

1. Shares held in a company in liquidation - period of holding shall commence from the date of acquisition and end with the date on which the company goes into liquidation.
2. Bonus shares - reckoned from the date of allotment of bonus shares and will end with the date of transfer.
3. Flat in a co-operative society - reckoned from the date of allotment of shares in the society and will end with the date of transfer.

Illustration 2

Examine, with reasons, whether the following statements are True or False.

1. Alienation of a residential house in a reverse mortgage transaction underneath an arrangement created and notified by the Central Government is regarded as a "transfer" for capital gains purposes.
2. Long-term capital assets will be zero coupon bonds of eligible corporations held for 14 months.

Solution

1. False
2. True

6.5 Basis of Charge

- Taxable in the previous year in which the asset is transferred

Scope and Year of Chargeability [SECTION 45]: General Provision

- Chargeable to Income-tax under this head in the previous year in which the transfer took place.
- The relevant date of transfer is not the date of the agreement to sell, but the actual date of sale
- However, Income-tax Act has recognized certain transactions as transfer in spite of the fact that conveyance deed might not have been executed and registered.



Example:

- Power of Attorney sales
- co-operative society transactions for acquisition of house are examples in this regard

Scope and Year of Chargeability Insurance Receipts [Section 45(1A)]

- Where any person receives any money or other assets under any insurance from an insurer, deemed to be the income of the such person for the previous year in which such money or other asset was received.

Scope and Year of Chargeability: Unit Linked Insurance Policy Receipts [Section 45(1B)]

- Where any person receives, at any time during any previous year, any amount, under a ULIP issued on or after 1.2.2021, to which exemption under section 10(10D) does not apply on account of -
 - Premium payable exceeding ` 2,50,000 for any of the previous years during the term of such policy; or
 - The aggregate amount of premium exceeding ` 2,50,000 in any of the previous years during the term of any such ULIP(s), in a case where premium is payable by a person for more than one ULIP issued on or after 1.2.2021,
 - Then, any profits or gains arising from receipt of such amount by such person shall be chargeable to income-tax under the head "Capital gains" and shall be deemed to be the income of the such person for the previous year in which such amount was received.
 - The income taxable shall be calculated in such manner as may be prescribed.

Scope and Year of Chargeability Conversion Or Treatment Of A Capital Asset As Stock-in-trade [Section 45(2)]

- Profits or gains arising from the above conversion or treatment will be chargeable to income-tax as his income of the previous year in which such stock-in-trade is sold or otherwise transferred by him.
- Capital gains
 - FMV on the date of conversion (-) Cost/Indexing Cost of acquisition/ improvement
 - Indexation benefit would be considered in relation to the year of conversion of capital asset into stock-in-trade
- Business Income
 - Sale price of stock-in- trade (-) FMV on the date of conversion

Compensation on compulsory acquisition [Section 45(5)]

- Such capital gains are chargeable as income of the previous year in which such compensation is received.
- Enhanced Compensation
 - The difference thereof will be chargeable to capital gains in the year in which the same is received from the government.

Compensation received in pursuance of an interim order deemed as income chargeable to tax in the year of final order

- Deemed to be income chargeable under the head 'Capital gains' in the previous year in which the final order of such Court, Tribunal or other authority is made.

Reduction of enhanced compensation

- Re-computation shall be done by way of rectification

Death of the transferor

- Chargeable to tax in the hands of the person who receives the same

Capital Gains on Distribution of Assets by Companies in Liquidation [Section 46]

- In the hands of liquidated company such distribution shall not be regarded as a transfer by the company for the purposes of section 45
- In the hands of shareholders
 - Distribution attributable to accumulated profits of the company:
 - Deemed dividend u/s 2(22) (c): Taxable in the hands of shareholders as "Income from Other Sources"

Money received (+) FMV of assets distributed (-) deemed dividend u/s 2(22) (c)

- To be considered for computing Capital Gains in the hands of shareholders

Capital Gains On Buyback of Shares or Specified Securities [Section 46A]**Taxability in the Hands of Company**

- **Buyback of specified securities by any company**
 - **Not taxable**
- **Buyback of shares by a company, other than a domestic company**
 - **Not taxable**
- **Buyback of shares by domestic companies**
 - **Subject to additional income- [tax@23.296%](#).**

Capital Gains On Buyback of Shares or Specified Securities [Section 46A]**Taxability in the hands of shareholder**

- **Buyback of specified securities by any company**
 - **taxable as capital gains u/s 46A.**
- **Buyback of shares by a company, other than a domestic company**
 - **taxable as capital gains u/s 46A.**
- **Buyback of shares by domestic companies**
 - **Exempt under section 10(34A)**

6.6 Transfer: What It Means? [Section 2(47)]

- the sale, exchange or relinquishment of the asset; or
- the extinguishment of any rights therein; or
- the compulsory acquisition thereof under any law; or
- the owner of a capital asset may convert the same into the stock-in-trade of a business carried on by him. Such conversion is treated as transfer; or
- the maturity or redemption of a zero coupon bond; or
- Part-performance of the contract: Sometimes, possession of an immovable property is given in consideration of part-performance of a contract.
- Lastly, there are certain types of transactions which have the effect of transferring or enabling the enjoyment of an immovable property

6.7 Transactions Not Regarded as Transfer (Sec. 46 & 47) Amended

- Any distribution of capital assets in the event of liquidation by a company to its shareholders shall not be treated as transfer in the hands of company. 46(1)
- Any distribution of capital assets on the total or partial partition of an HUF. 47(i)
- Any transfer of a capital asset under a gift or will or an irrevocable trust 47(iii)
 - Exception: Gift of shares acquired through Employees Stock Option Plan (ESOP) shall be treated as Transfer
- Any transfer of a capital asset by a 100% holding company to its Indian subsidiary company. 47(iv)
- Any transfer of a capital asset by a 100% subsidiary company to its Indian holding company 47(v)
- Any transfer, in a scheme of amalgamation, of a capital asset by the amalgamating company to the amalgamated company if the amalgamated company is an Indian company. 47(vi)
- Any transfer, in a scheme of amalgamation, of a capital asset being a share or shares held in an Indian company, by the amalgamating foreign company to the amalgamated foreign company, if -
 - At least 25% of the shareholders of the amalgamating foreign company continue to remain shareholders of the amalgamated foreign company; and
 - Such transfer does not attract tax on capital gains in the country, in which the amalgamating company is incorporated 47(via)
- Any transfer of a capital asset by a banking company to a banking institution in a scheme of amalgamation of such banking company with such banking institution sanctioned and brought into force by the Central Government u/s 45(7) of the Banking Regulation Act, 1949.
- Any transfer, in a scheme of amalgamation, of a capital asset, being a share of a foreign company, (referred to in the Explanation 5 of sec.9(1)(i)), which derives, directly or indirectly, its value substantially from the share or shares of an Indian company, held by the amalgamating foreign company to the amalgamated foreign company, if:
 - i. At least 25% of the shareholders of the amalgamating foreign company continue to remain shareholders of the amalgamated foreign company; and
 - ii. Such transfer does not attract tax on capital gains in the country in which the amalgamating company is incorporated 47(via b)
- Any transfer of capital asset by India Infrastructure Finance Company Ltd to an institution established for financing the infrastructure and development, set up under an Act of Parliament and notified by the Central Government. 47(vii ae)
- Any transfer of capital asset, under a plan approved by the Central Government, by a public sector company to another notified public sector company or to the Central Government or to a State Government. 47(vii af)
- Any transfer, in a scheme of demerger, of capital asset by the demerged company to the resulting company, if the resulting company is an Indian company 47(vi b)
 1. Any transfer, in a scheme of demerger, of a capital asset, being a share or shares held in an Indian company, by the demerged foreign company to the resulting foreign company, if -
 2. The shareholders holding not less than three-fourths in value of the shares of the demerged foreign company continue to remain shareholders of the resulting foreign company; and
 3. Such transfer does not attract tax on capital gain in the country, in which the demerged foreign company is incorporated:

Income Tax Law and Practice

- any transfer in a business reorganisation, of a capital asset by the predecessor co-operative bank to the successor co-operative bank or to the converted banking company 47(vi ca)
- Any transfer by a shareholder, in a business reorganization, of a capital asset being a share or shares held by him in the predecessor co-operative bank if the transfer is made in consideration of the allotment to him of any share or shares in the successor co-operative bank or to the converted banking company 47(vi cb)
- Any transfer in a demerger, of a capital asset, being a share of a foreign company (referred to in the Explanation 5 of sec. 9(1)(i)), which derives, directly or indirectly, its value substantially from the share or shares of an Indian company, held by the demerged foreign company to the resulting foreign company, if:
 - i. The shareholders, holding not less than 3/4th in value of the shares of the demerged foreign company, continue to remain shareholders of the resulting foreign company; and
 - ii. Such transfer does not attract tax on capital gains in the country in which the demerged foreign company is incorporated. 47(vi cc)
- iii. Any transfer or issue of shares by the resulting company, in a scheme of demerger to the shareholders of the demerged company if the transfer or issue is made in consideration of demerger of the undertaking. 47(vi d)
- Any transfer by a shareholder, in a scheme of amalgamation, of share(s) held by him in the amalgamating company, if –
 - i. The transfer is made in consideration of the allotment to him of any share or shares in the amalgamated company except where the shareholder itself is the amalgamated company, and
 - ii. The amalgamated company is an Indian company 47(vii)
- Any transfer of a capital asset, being foreign currency convertible bonds or Global Depository Receipts referred to in sec. 115AC (1), made outside India by a non-resident to another nonresident. 47(vii a)
- Any transfer, made outside India, of a capital asset being rupee denominated bond of an Indian company issued outside India, by a non-resident to another non-resident 47(vii aa)
- Any transfer of a capital asset, being –
 - i. bond or Global Depository Receipt referred to in sec. 115AC(1); or
 - ii. rupee denominated bond of an Indian company; or
 - iii. derivative, or
 - iv. other notified securities made by a non-resident on a recognised stock exchange located in any International Financial Services Centre provided the consideration for such transaction is paid or payable in foreign currency. 47(vii ab)
- Any transfer of a capital asset, being a Government Security carrying a periodic payment of interest, made outside India through an intermediary dealing in settlement of securities, by a non-resident to another non-resident 47(vii b)
- Any transfer of Sovereign Gold Bond issued by the RBI under the Sovereign Gold Bond Scheme, 2015, by way of redemption, by an assessee being an individual. 47(vii c)
- Any transfer of a capital asset being a work of art, archaeological, scientific or art collection, book, manuscript, drawing, painting, photograph or print, to the Government or a University or the National Museum, National Art Gallery, National Archives or any such other public museum or institution as may be notified by the Central Government in the Official Gazette to be of national importance or to be of renown throughout any State or States. 47(ix)
- Any transfer by way of conversion of bonds or debentures, debenture-stock or deposit certificates in any form of a company into shares or debentures of that company. 47(x)

Unit 06: Computation of Income under the Head Capital Gains

- Any transfer by way of conversion of bonds referred to in sec. 115AC(1)(a) into shares or debentures of any company 47(x a)
- Any transfer by way of conversion of preference shares of a company into equity shares of that company 47(xb)
- Any transfer of a land of a sick industrial company, made under a scheme prepared and sanctioned u/s 18 of the Sick Industrial Companies (Special Provisions) Act, 1985 where such sick industrial company is being managed by its workers' co-operative.
 - i. Such transfer must have been made during the period commencing from the previous year in which the said company has become a sick industrial company and ending with the previous year during which the entire net worth of such company becomes equal to or exceeds the accumulated losses. 47(xii)
- Any transfer of a capital asset by a firm to a company as a result of succession of the firm by a company in the business carried on by the firm subject to following conditions:
 - i. All assets and liabilities of the firm relating to the business immediately before the succession become the assets and liabilities of the company.
 - ii. All the partners of the firm immediately before the succession become the shareholders of the company in the same proportion in which their capital accounts stood in the books of the firm on the date of succession.
 - iii. The partners of the firm do not receive any consideration or benefit, directly or indirectly, in any form or manner, other than by way of allotment of shares in the company; and
 - iv. The aggregate of the shareholding in the company of the partners of the firm is not less than 50% of the total voting power in the company and their shareholding continues to be as such for a period of 5 years from the date of succession. 47(xiii)
- Any transfer of a membership right of a recognized stock exchange in India for acquisition of shares and trading or clearing rights in that recognized stock exchange in accordance with a scheme for demutualisation or corporatisation which is approved by SEBI
- 47(xiii b) Any transfer of -
 - a capital asset or intangible asset by a private company or unlisted public company (hereafter referred to as the company) to a limited liability partnership (LLP); or
 - a share(s) held in the company by a shareholder as a result of conversion of the company into a limited liability partnership (LLP) shall not be regarded as a transfer, if following conditions are satisfied:
 - All the assets and liabilities of the company immediately before the conversion become the assets and liabilities of the LLP;
 - All the shareholders of the company immediately before the conversion become the partners of the LLP and their capital contribution and profit sharing ratio in the LLP are in the same proportion as their shareholding in the company on the date of conversion;
 - The shareholders of the company do not receive any consideration or benefit other than by way of share in profit and capital contribution in the LLP;
 - The aggregate of the profit sharing ratio of the shareholders of the company in the LLP shall not be less than 50% at any time during the period of 5 years from the date of conversion;
 - The total sales, turnover or gross receipts in business of the company in any of the 3 previous years preceding the previous year in which the conversion takes place does not exceed ₹ 60 lakh;

Income Tax Law and Practice

- The total value of the assets as appearing in the books of account of the company in any of the 3 previous years preceding the previous year in which the conversion takes place does not exceed ` 5 crore; and
- No amount is paid (directly or indirectly) to any partner out of balance of accumulated profit standing in the accounts of the company on the date of conversion for a period of 3 years from the date of conversion.
- Where a sole proprietary concern is succeeded by a company in the business carried on by it as a result of which the sole proprietary concern sells or otherwise transfers any capital asset to the company, subject to following conditions –
 - i. All assets and liabilities of the sole proprietary concern relating to the business immediately before the succession become the assets and liabilities of the company;
 - ii. Proprietor holds not less than 50% of the total voting power in the company and his shareholding continues to remain as such for a period of 5 years from the date of succession; and
 - iii. The sole proprietor does not receive any consideration or benefit, directly or indirectly, in any form or manner, other than by way of allotment of shares in the company. 47(xiv)
- Any transfer in a scheme for lending of any securities under an agreement or arrangement, which the assessee has entered into with the borrower of such securities and which is subject to the guidelines issued by the SEBI or the RBI. 47(xv)
- Any transfer of a capital asset in a transaction of reverse mortgage under a scheme made and notified by the Central Government 47(xvi)
- Any transfer of a capital asset, being share of a special purpose vehicle (referred to in sec. 10(23FC)) to a business trust in exchange of units allotted by that trust to the transferor 47(xvii)
- Any transfer by a unit holder of a capital asset, being a unit or units, held by him in the consolidating scheme of a mutual fund, made in consideration of the allotment to him of a capital asset, being a unit or units, in the consolidated scheme of the mutual fund.
 - The exemption is available only the consolidation of two or more schemes of equity oriented fund or of two or more schemes of a fund other than equity oriented fund. 47(xviii)
- In the case of a capital asset, being a unit or units, which becomes the property of the assessee in consideration of a transfer referred to in this clause, period of holding shall include the period for which the unit or units in the consolidating scheme of the mutual fund were held by the assessee. 47(xviii)
- Any transfer by a unit holder of a capital asset, being a unit or units, held by him in the consolidating plan of a mutual fund scheme, made in consideration of the allotment to him of a capital asset, being a unit or units, in the consolidated plan of that scheme of the mutual fund 47(xix)

6.8 Computation of Capital Gains [SEC. 48]

- Short-term Capital Gain means the gain arising on the transfer of short-term capital asset [Sec. 2(42B)].
- Long-term Capital Gain means the gain arising on the transfer of long-term capital assets [Sec. 2(29B)].

Short-term Capital Gain

Sale consideration (Full value of consideration)

Less: Expenses on transfer

Unit 06: Computation of Income under the Head Capital Gains

Net sale consideration

Less:

- i) Cost of acquisition
- ii) Cost of improvement

Short Term Capital Gain

- Less: Exemption u/s 54B, 54D, 54G, etc.

Taxable Short Term Capital Gain

Illustration 1

- Mr. D had purchased jewellery as on 17/8/2020 for 20,000.
- On 1/05/2021, he improved on it costing, 25,000.
- On 1/08/2021, he sold such jeweller for 80,000
- Incurred brokerage for arranging customer 5,000.
- Compute capital gain

Sale consideration	80,000
Less: Expenses on transfer	5,000
Net sale consideration	75000
Less:	
i) Cost of acquisition	20000
ii) Cost of improvement	25000
STCG	30000

Computation of Long Term Capital Gain (LTCG)

Sale consideration
Less: Expenses on transfer
Net sale consideration
Less:
i) Indexed Cost of acquisition
ii) Indexed Cost of improvement
LTCG

Indexed Cost of Acquisition and Improvement

- Indexed cost of acquisition =

Cost of acquisition × Index of the year of transfer/ Index of the year of acquisition

Income Tax Law and Practice

- Indexed cost of improvement =

Cost of improvement × Index of the year of transfer/ Index of the year of improvement

Cost Inflation Index

- Cost Inflation Index (CII) is used to estimate the increase in the prices of goods and assets year by year due to inflation.
- The Cost Inflation Index (CII) for the financial year 2022-23 is 331.

Why is Cost Inflation Index calculated

- Cost Inflation Index is calculated to match the prices to the inflation rate.
- The cost inflation index is applied to the long-term capital assets only.

What is the concept of the base year in Cost Inflation Index?

- The base year is the first year of the cost inflation index and has an index value of 100.
- The index of all other years is compared to the base year to see the increase in inflation percentage.

Cost Inflation Index (CII)

Financial Year	Cost Inflation Index (CII)
2001-02 (Base year)	100
2002-03	105
2003-04	109
2004-05	113
2005-06	117
2006-07	122
2007-08	129
2008-09	137
2009-10	148
2010-11	167
2011-12	184
2012-13	200
2013-14	220
2014-15	240
2015-16	254
2016-17	264
2017-18	272
2018-19	280

Unit 06: Computation of Income under the Head Capital Gains

2019-20	289
2020-21	301
2021-22	317
2022-23	331

Why is the base year of Cost Inflation Index changed to 2001 from 1981

- Initially, 1981-82 was considered as the base year.
- But, taxpayers were facing hardships in getting the properties valued which were purchased before 1st April 1981.
- Tax authorities were also finding it difficult to rely on the valuation reports.
- Hence, the government decided to shift the base year to 2001 so that valuations can be done quickly and accurately.

Treatment of assets acquired before 1/4/2001

- **Cost of acquisition:**
- If an asset is acquired before 1/4/2001, then its cost of acquisition shall be higher than the following:
 - a) Actual cost of acquisition (ignoring cost of improvement incurred before 1/4/2001), or
 - b) Fair market value of the asset as on 1/4/2001 [Sec. 55]

Exception:

- The option is not available in case of -
 - Asset on which depreciation is allowed u/s 32(1)(ii);
 - Self-generated assets (other than bonus share)
- **Cost of improvement**
 - Any cost of improvement incurred by the assessee or the previous owner before 1/4/2001 shall not be considered.
- Indexation
 - Where an asset is acquired before 1/4/2001, then indexation benefit shall be available from the year 2001-02.

Illustration3

- On 23rd December 2021, R sold 500 grams of gold, the sale consideration of which was 13,50,000.
- He had acquired this gold on 20th August 2000 for 4,00,000.
- Fair market value of 500 grams of gold on 1st April 2001 was 3,60,000.
- Find out the amount of capital gain chargeable to tax for the assessment year 2022-23.

Solution:

Sale consideration	13,50,000
Less: Expenses on transfer	
Net sale consideration	13,50,000
Less:	

Income Tax Law and Practice

i) Indexed Cost of acquisition	
$4,00,0001 \times 317/100$	12,68,000
LTCG	82,000

Illustration 4

- Mr. A has purchased a house property on 17/08/2002 for 5,00,000.
- On 1/05/2004, he constructed a new floor on the same house at the cost of 2,50,000.
- On 1/10/2021, he sold the such house for 18,00,000
- incurred brokerage @ 2% for arranging customer.
- Compute capital gain.

Solution

Sale consideration	18,00,000
Less: Expenses on transfer(2% of 18,00,000)	36,000
Net sale consideration	17,64,000
Less:	
i) Indexed Cost of acquisition	
$5,00,000 \times (317/105)$	(15,09,524)
ii) Indexed Cost of improvement	
$2,50,000 \times (317/113)$	(7,01,327)
LTCG	(4,46,851)

Deemed or Notional Cost of Acquisition [SEC. 49(1)]

Cost of acquisition of the previous owner of the property shall be deemed to be the cost of acquisition for the assessee:

- Assets received on the total or partial partition of HUF [Sec. 49(1)(i)].
- Assets received under a gift or will [Sec. 49(1)(ii)].
- Assets received by succession, inheritance, or devolution [Sec. 49(1)(iii)(a)].
- Assets received on dissolution of a firm, BOI or AOP [Sec. 49(1)(iii)(b)].
- Assets received on liquidation of a company [Sec. 49(1)(iii)(c)].
- Assets received under a trust (whether revocable or irrevocable) [Sec. 49(1)(iii)(d)].
- Assets received under business reorganization are subject to certain conditions [Sec. 49(1)(iii)(e)] e.g., assets received by a 100% Indian subsidiary company from its holding company or received by an Indian holding company from its 100% subsidiary company or received by an amalgamated Indian company from the amalgamating company, the asset received on the conversion of a company into LLP, etc.
- Asset (being a self-acquired property of a member) received by a HUF from its member [Sec. 49(1)(iv)]

6.9 Exemptions u/s 54

- Deduction from capital gain on sale of residential house property [sec. 54]
- Deduction from capital gain on compulsory acquisition of land and building forming part of industrial undertaking [sec. 54d]
- Deduction from capital gain on acquisition of certain bonds [sec. 54ec].
- Deduction from capital gain on investment in units of a specified fund [sec. 54ee].
- Deduction from capital gain on transfer of capital assets other than residential house property [sec. 54f]
- Deduction from capital gain on transfer of capital assets in case of shifting of industrial undertaking from urban areas [sec. 54g]
- Deduction from capital gain on transfer of agro land [sec. 54b]
- Deduction from capital gain on transfer of capital assets in case of shifting of industrial undertaking from urban areas to special economic zone [sec. 54ga]
- Deduction from capital gain on transfer of residential property for investment in eligible company [sec. 54gb] amended.

Summary

Incomes from the transfer of capital assets are subject to the provisions for calculating income from capital gains. The Income-tax Act of 1961's Sections 45 through 55A address capital gains. According to Section 45 of the Act, profits or gains from the sale of a capital asset in the prior year are subject to income tax under the heading "Capital Gains" and are considered to be part of the previous year's income, unless otherwise provided in Sections 54, 54B, 54D, 54EC, 54ED, 54F, 54G, 54GA, and 54H. The transfer of a "capital asset" is a necessary condition for the imposition of tax on capital gains. - Short-term capital gain is any capital gain that results from the transfer of a short-term capital asset. Capital assets that have been held by an assessee for less than 36 months before to the date of transfer are referred to as "short term" assets. When a taxpayer holds capital assets (i.e., stock or preferred shares in a firm) for no longer than 12 months prior to a transfer. Under certain conditions, capital gains on the transfer of specific capital assets are excluded from taxation under Sections 54, 54B, 54D, 54EC, 54F, 54G, and 54H of the Act.

Keywords

"Consolidated scheme" means the scheme with which the consolidating scheme merges or which is formed as a result of such merger.

"Consolidating scheme" means the scheme of a mutual fund which merges under the process of consolidation of the schemes of mutual fund in accordance with the Securities and Exchange Board of India (Mutual Funds) Regulations, 1996 made under the Securities and Exchange Board of India Act, 1992.

"capital asset" to means Property of any kind held by an assessee whether or not connected with his business or profession but does not include any stock-in-trade, personal effects, agricultural land in India, 6[^] per cent Gold Bonds, Special Bearer Bonds, Gold Deposit Bonds.

SelfAssessment

1. Mr. Raja paid Rs. 84,000 for purchasing a plot of land in May 2005, and then sold it for Rs. 10,10,000 in April 2021. (brokerage Rs. 10,000). What kind of capital gain will be taxable in Mr. Raja's hands? The method for calculating capital gains is as follows:
 - A. Long-Term Capital Gains 7,83,897
 - B. Short-Term Capital Gains 7,83,897
 - C. Long-Term Capital Gains 10,00,000
 - D. Short-Term Capital Gains 10,00,000

2. Mr. Janak works for a salary. He bought 100 shares of X Ltd. in January 2016 from the Bombay Stock Exchange for Rs. 1,400 each share. In April 2022, these shares were sold on the BSE for Rs. 2,600 each. On January 31, 2018, X Ltd. shares were valued at a high of Rs. 1,800 per share on the stock exchange.
- Cost of acquisition of shares shall be:
- A. 1,00,000
 - B. 1,80,000
 - C. 2,60,000
 - D. 1,40,000
3. Mr. Janak works for a salary. He bought 100 shares of X Ltd. in January 2016 from the Bombay Stock Exchange for Rs. 1,400 each share. In April 2022, these shares were sold on the BSE for Rs. 2,600 each. On January 31, 2018, X Ltd. shares were valued at a high of Rs. 1,800 per share on the stock exchange. How much long term Capital gain will there be in this situation?
- A. 80,000
 - B. 1,80,000
 - C. 2,60,000
 - D. 1,40,000
4. Mr. Janak works for a salary. He bought 100 shares of X Ltd. in January 2016 from the Bombay Stock Exchange for Rs. 1,400 each share. In April 2022, these shares were sold on the BSE for Rs. 2,600 each. On January 31, 2018, X Ltd. shares were valued at a high of Rs. 1,800 per share on the stock exchange. Since transaction is liable to STT, Section is applicable in this case
- A. 121A
 - B. 112A
 - C. 113B
 - D. 114C
5. Mr. Saurabh works for a salary. He bought 100 shares of XYZ Ltd. in the month of July 2017 from the Bombay Stock Exchange for Rs. 2,000 per share. In June 2022, these shares were sold on the NSE for Rs. 4,900 each. On January 31, 2018, XYZ Ltd. shares reached their highest quoted price of Rs. 3,800 per share on the stock exchange. How much capital gain will there be in this situation?
- A. LTCG 1,10,000
 - B. STCG 1,10,000
 - C. LTCG 3,80,000
 - D. STCG 3,80,000
6. Mr. Saurabh works for a salary. He bought 100 shares of XYZ Ltd. in the month of July 2017 from the Bombay Stock Exchange for Rs. 2,000 per share. In June 2022, these shares were sold on the NSE for Rs. 4,900 each. On January 31, 2018, XYZ Ltd. shares reached their highest quoted price of Rs. 3,800 per share on the stock exchange. How much cost of acquisition will there be in this situation?
- A. 1,10,000

Unit 06: Computation of Income under the Head Capital Gains

- B. 3,80,000
C. 4,90,000
D. 1,00,000
7. Mr. Saurabh works for a salary. He bought 100 shares of XYZ Ltd. in the month of July 2017 from the Bombay Stock Exchange for Rs. 2,000 per share. In June 2022, these shares were sold on the NSE for Rs. 4,900 each. On January 31, 2018, XYX Ltd. shares reached their highest quoted price of Rs. 3,800 per share on the stock exchange. Mr. Saurabh would be liable to pay at the rate of ...% in this situation?
- A. 15
B. 20
C. 10
D. 30
8. Mr. Saurabh works for a salary. He bought 100 shares of XYZ Ltd. in the month of July 2017 from the Bombay Stock Exchange for Rs. 2,000 per share. In June 2022, these shares were sold on the NSE for Rs. 4,900 each. On January 31, 2018, XYX Ltd. shares reached their highest quoted price of Rs. 3,800 per share on the stock exchange. Mr. Saurabh would be liable to pay at the prescribed rate on in this situation?
- A. 10,000
B. 1,00,000
C. 110000
D. 3,80,000
9. In December 1995, Mr. Kumar, a non-resident, paid Rs. 28,100 for equity shares (listed) in Shyamal Ltd. In April 2022, these shares are sold for Rs. 5,000 (off a recognized stock exchange). He has no other sources of income that are taxable in India. What will his tax obligation be in case he (Avail indexation)?
- A. 28,100
B. 47,190
C. 83,084
D. 84,581
10. In December 1995, Mr. Kumar, a non-resident, paid Rs. 28,100 for equity shares (listed) in Shyamal Ltd. In April 2022, these shares are sold for Rs. 5,000 (off a recognized stock exchange). He has no other sources of income that are taxable in India. What will his tax obligation be in case he (Does not Avail indexation)?
- A. 28,100
B. 47,190
C. 83,084
D. 84,581
11. In December 1995, Mr. Kumar, a non-resident, paid Rs. 28,100 for equity shares (listed) in Shyamal Ltd. In April 2022, these shares are sold for Rs. 5,000 (off a recognized stock exchange). He has no other sources of income that are taxable in India. What will his cost of acquisition be in case he (Does not Avail indexation)?
- A. 28,100

- B. 47,190
C. 83,084
D. 84,581
12. In December 1995, Mr. Kumar, a non-resident, paid Rs. 28,100 for equity shares (listed) in Shyamal Ltd. In April 2022, these shares are sold for Rs. 5,000 (off a recognized stock exchange). He has no other sources of income that are taxable in India. What will his cost of acquisition be in case he (Avail indexation)?
A. 28,100
B. 47,190
C. 83,084
D. 84,581
13. In December 1995, Mr. Kumar, a non-resident, paid Rs. 28,100 for equity shares (listed) in Shyamal Ltd. In April 2022, these shares are sold for Rs. 5,000 (off a recognized stock exchange). He has no other sources of income that are taxable in India. What will his taxable income be in case he (Avail indexation).
A. 28,100
B. 47,190
C. 4,71,900
D. 4,15,419
14. In December 1995, Mr. Kumar, a non-resident, paid Rs. 28,100 for equity shares (listed) in Shyamal Ltd. In April 2022, these shares are sold for Rs. 5,000 (off a recognized stock exchange). He has no other sources of income that are taxable in India. What will his taxable income be in case he (Does not Avail indexation).
A. 28,100
B. 47,190
C. 4,71,900
D. 4,15,419
15. In December 1995, Mr. Kumar, a non-resident, paid Rs. 28,100 for equity shares (listed) in Shyamal Ltd. In April 2022, these shares are sold for Rs. 5,000 (off a recognized stock exchange). He has no other sources of income that are taxable in India. Which option should he exercise?
A. Avail indexation
B. Does not Avail indexation
C. He is not taxable at all
D. He is not eligible to exercise any of the options

Answers for Self Assessment

- | | | | | |
|-------|-------|-------|-------|-------|
| 1. A | 2. B | 3. A | 4. B | 5. A |
| 6. B | 7. C | 8. A | 9. C | 10. B |
| 11. A | 12. D | 13. D | 14. C | 15. B |

Review Questions

- i. What prerequisites must be met before income falling under the heading of capital gains is taxable?
- ii. In general, capital gains are taxed in the year of the transfer of the capital asset. Exist any glaring exceptions to the rule?
- iii. The long-term capital asset is indexed. Exist any exceptions to the rule?
- iv. Is the conversion of a capital asset into stock subject to capital gains taxes?
- v. When all of a division's assets and liabilities are sold for a single sum of money without having a price assigned to each one individually, how will capital gain be calculated?



Further Readings

- https://www.icsi.edu/media/webmodules/16112021_Advance_Tax_Laws.pdf
- Income Tax Law & Practice A.Y 2021-22 by Dr H.C. Mehrotra and Dr. S. P. Goyal. Sahitya Bhawan Publications
- Study Material on Direct Tax Laws and International Taxation by ICAI
- Direct Tax Laws and Practice by Dr. Girish Ahuja & Dr. Ravi Gupta
- <https://incometaxindia.gov.in/tutorials/15-%20ltcg.pdf>

Unit 07: Computation of Income under the Head Business & Profession

CONTENTS

Objectives

Introduction

7.1 Meaning of business & profession

7.2 Income chargeable under the head profits and gains of business or profession [sec. 28]

7.3 Incomes not taxable under the head profits and gains of business or profession

7.4 Expenditures allowed as deduction: Specific Deductions

7.5 Meaning of Book profit

Summary

Keywords

Self Assessment

Answers for Self Assessment

Review Questions

Further Readings

Objectives

After studying this unit, you will be able to:

- understand the difference Between Business and Profession.
- distinguish between Allowable and Disallowed Expenses.
- Understand computation of Book Profits
- Understand computation of total Income Under the Head Business and Profession

Introduction

“Profit and gains of business or profession” is one of the heads of income under the Income Tax Act. For the purpose of ascertaining the tax liability of a taxpayer, the Income Tax Act divides the taxable income of an assessee into five categories or heads of income. Business profits is the third head of income under the Act, after salaries and house property income. This head is used to classify or aggregate income which the taxpayer generates through business or professional activities. While filing an income tax return, the taxpayer must declare the amount of profits and gains of business or profession in case the assessee is having any such income. In this article, we mention the procedure for calculating Profits and Gains of Business or Profession.

7.1 Meaning of business & profession

Business [Sec. 2(13)]

Business includes –

- a. any trade, commerce or manufacture; or
- b. any adventure or concern in the nature of trade, commerce or manufacture.

Profession [Sec. 2(36)]

- Profession includes vocation
 - Profession requires purely intellectual skill or manual skill on the basis of some special learning and qualification gathered through past training or experience.
 - Professional skill can be acquired only after patient study and application.
- Vocation
 - Natural ability of a person to do some particular work.
 - Earning feature.
 - Does not require a degree or special learning.

Meaning of 'Profits'

- Profits in cash or in kind:
 - Profits may be realized in money or in money's worth, i.e., in cash or in kind
- Capital receipts:

Capital receipts are not generally to be taken into account while computing profits under this head

- Voluntary Receipts:
 - Payment voluntarily made by persons who were under no obligation to pay anything at all would be income in the hands of the recipient, if they were received in the course of a business or by the exercise of a profession or vocation
- Application of the gains of trade is immaterial:
 - Gains made even for the benefit of the community by a public body would be liable to tax.
- Legality of income:
 - The illegality of a business, profession or vocation does not exempt its profits from tax.
- Income from distinct businesses:
 - The profits of each distinct business must be computed separately but the tax chargeable under this section is not on the separate income of every distinct business but on the aggregate profits of all the business carried on by the assessee.
- Computation of profits:
 - Profits should be computed after deducting the losses and expenses incurred for earning the income in the regular course of the business, profession, or vocation unless the loss or expenses is expressly or by necessary implication, disallowed by the Act.

7.2 Income chargeable under the head profits and gains of business or profession [sec. 28]

- Profits & gains of any business or profession [Sec. 28(i)]
- Income of trade or professional association's [Sec. 28(iii)]
- Export incentive [Sec. 28(iii) (iib) & (iic)]
- Remuneration to partner [Sec. 28(v)]:
- Amount received or receivable for certain agreement [Sec. 28(v a)]:
- Perquisite from business or profession [Sec. 28(iv)]
- Compensation to Management agency [Sec. 28(ii)]

Compensation to Management agency [Sec. 28(ii)]

- Any compensation/other payment due to or received by:
 - Any person managing the affairs of an Indian company
 - Any person managing the affairs of any company in India
- In connection with:
 - Termination or modification of terms and conditions of his appointment

Unit 07: Computation of Income under the Head Business & Profession

- Any compensation/other payment due to or received by:
 - Any person holding an agency in India for any part of the activities relating to the business of any other person
 - In connection with:
 - Termination of agency or the modification of terms and conditions in relation thereto.
- Any compensation/other payment due to or received by:
 - Any person holding an agency in India for any part of the activities relating to the business of any other person
 - In connection with:
 - Termination of agency or the modification of terms and conditions in relation thereto.
- Any compensation/other payment due to or received by:
 - Any person
 - In connection with:
 - The vesting in the Government or in any corporation owned/controlled by the Government, of the management of any property or business.
- Any compensation/other payment due to or received by:
 - Any person
 - In connection with:
 - The termination or the modification of the terms and conditions, of any contract relating to his business.

Income of trade or professional association's [Sec. 28(iii)]:

Income derived by a trade, professional or similar association from rendering specific services to its members shall be taxable under this head.

Note: This is an exception to the general principle that a surplus of mutual association cannot be taxed

Export incentive [Sec. 28(iii a) (iii b)]& (iii c)]:

- An export incentive in form of -
 - Profit on sale of import license or duty entitlement pass book. [Sec. 28(iii a)/(iii d)/(iii e)]
 - Cash assistance received/receivable by an exporter under a scheme of the Government of India [Sec. 28(iii b)] •Duty draw back (received/receivable) for export e.g. duty drawback, etc. [Sec. 28(iii c)]

Perquisite from business or profession [Sec. 28(iv)]:

- The value of any benefit or perquisite, whether convertible into money or not, arising from business or profession shall be taxable under this head.

Amount received or receivable for certain agreement [Sec. 28(v a)]:

- Any sum, whether received or receivable in cash or in kind, under an agreement for -
 - not carrying out any activity in relation to any business or profession; or
 - not sharing any know-how, patent, copyright, trade mark, license, franchise or any other business or commercial right of similar nature or information or technique likely to assist in the manufacture or processing of goods or provisions for services.
- Exceptions: The aforesaid provision is not applicable in respect of the following:
 - a. any sum received or receivable in cash or in kind on account of transfer of the right to manufacture, produce or process any article or thing; or right to carry on any business or profession, which is chargeable under the head Capital gains;

- b. any sum received as compensation from the multilateral fund of the Montreal Protocol on Substances that Deplete the Ozone Layer under the United Nation Environment Programme, in accordance with the terms of agreement (whether or not in writing, whether or not intended to be enforceable by legal proceedings) entered into with the Government of India

Keyman Insurance Policy [Sec. 28(vi)]:

Any sum received under a Keyman Insurance Policy including bonus on such policy.

- As per sec. 10(10D) Keyman insurance policy is a life insurance policy taken by a person on the life of another person who is or was –
- an employee of the first mentioned person; or
- in any manner whatsoever connected with the business of the first-mentioned person.
- and includes such policy which has been assigned to a person, at any time during the term of the policy, with or without any consideration

Conversion of stock into capital asset [Sec. 28(via)]:

- The fair market value of inventory as on the date on which it is converted into, or treated as, a capital asset.

Recovery against certain capital assets covered u/s 35AD [Sec. 28(vii)]:

- Any sum received or receivable (in cash or kind) on account of any capital asset (other than land or goodwill or financial instrument) being demolished, destroyed, discarded, or transferred if the whole of the expenditure on such capital asset has been allowed as a deduction u/s 35AD.

General Points

- Legality of business immaterial
- Compilation of income of all businesses or profession:
- Business or profession must be carried on during the previous year

Exceptions

- Where any business or profession is discontinued in any year and any sum received after the discontinuance:
- The sum so received shall be deemed to be the income of the recipient & charged to tax accordingly in the year of receipt, if such sum would have been included in the total income of the person who carried on the business had such sum been received before such discontinuance.

7.3 Incomes not taxable under the head profits and gains of business or profession

- Rent from house property is taxable u/s 22 under 'Income from house property' even though the assessee is engaged in the business of letting out properties on rent; or such property is held as stock in trade

Note: However, where letting of house supporting the smooth running of the business (i.e. incidental to business), then such income shall be taxable under this head.

- Dividend on shares is taxable u/s 56(2)(i) under the head 'Income from other sources' even though the assessee deals in shares and such shares are held as stock in trade.
- The provision is not applicable in case of interest on securities held as stock in trade.

Unit 07: Computation of Income under the Head Business & Profession

- Winning from lotteries, races etc. are taxable under the head 'Income from other sources' even if such income is derived through regular business activity.
- Exempted income by virtue of sec. 10, 11 or 13A.
- Sum taxable under the head 'Capital gains' for the purpose of sec. 28 (v a) shall not be taxable under this head.

7.4 Expenditures allowed as deduction: Specific Deductions

RENT, RATES, TAXES, REPAIRS AND INSURANCE FOR BUILDING [SEC. 30]:

1. Use of building:
2. Notional Rent:
3. Current repair vs Capital repair:
4. Municipal taxes

In respect of rent, rates, taxes, repairs and insurance for premises, used for the purposes of the business or profession, the following deductions shall be allowed -

(a) where the premises are occupied by the assessee -

- i. as a tenant, the rent paid for such premises; and further if he has undertaken to bear the cost of repairs to the premises, the amount paid on account of such repairs;
- ii. otherwise than as a tenant, the amount paid by him on account of current repairs to the premises;

(b) any sums paid on account of land revenue, local rates or municipal taxes subject to the provision of section 43B;

(c) the amount of any premium paid in respect of insurance against risk of damage or destruction of the premises.

Repairs and insurance of machinery, plant and furniture [sec. 31]

Repairs & insurance of plant, machinery & furniture are allowed as deduction. Points to be noted in this regard:

1. Use of asset
2. Current repair vs Capital repair
3. Rent for furniture, plant or machinery

In respect of repairs and insurance of machinery, plant or furniture used for the purposes of the business or profession, the following deductions shall be allowed -

- i. the amount paid on account of current repairs thereto ;
- ii. the amount of any premium paid in respect of insurance against risk of damage or destruction thereof.
- iii. In order to avail deduction, it is mandatory that plant, machinery, or furniture must be utilized for the purpose of assessee's business during the previous year. It is however not necessary that these assets should be used throughout the previous year - CIT v. National Syndicate [1961] 41 ITR 225(SC).

Scientific research [sec. 35]

Such research can be categorised either as -

- a. In-House research: Research done by the assessee himself (in connection with his business)
- b. Research through outside institutions: Any sum paid to outside agencies, engaged in scientific research, to be used for scientific research

a) In-House research

- Revenue expenditure sec. 35(1)(i)
 - After commencement of business:
 - Where the assessee himself carries on scientific research related to his business and incurs revenue expenditure, such expenses are allowed as deduction in the year in which such expenditure is incurred by the assessee
 - Before commencement of business
 - Following revenue expenditures (certified by the prescribed authority) incurred during 3 years immediately before commencement of business, shall be allowed as deduction in the year of commencement of business –
 - Payment of salary to an employee engaged in scientific research (excluding perquisite).
 - Purchase of materials used for scientific research
- Capital Expenditure sec.35(1)(iv) / sec.35(2)
 - After commencement of business:
 - Any capital expenditure incurred (other than land) for scientific research, related to the business of the assessee, will be allowed as deduction in full.
 - Before commencement of business
 - Any capital expenditure incurred (other than land) during 3 years immediately preceding the year of commencement of business shall be deemed to have been incurred in the year in which the business commenced and is allowed as deduction in that year

b) Research through outside institutions

- Deduction @ 100% shall be allowed in respect of expenditure on Research through following outside institution:
 - Any payment to National Laboratory or a University or Indian Institute of Technology or a specified person. [Sec. 35(2AA)]
 - Purpose: Scientific research undertaken under programme approved by the prescribed authority (whether related to business or not)
- Deduction @ 100% shall be allowed in respect of expenditure on Research through following outside institution:
 - Any payment made to a notified (by the Central Government) research association, university, college or other institution [Sec. 35(1)(iii)].
 - Purpose: Research in Social science or Statistical Research (whether related to business or not)
- Deduction @ 100% shall be allowed in respect of expenditure on Research through following outside institution:
 - Any payment to an approved Indian company (main object of whom is scientific research & development) [Sec. 35(1)(ii a)].
 - Purpose: Scientific research (whether related to business or not)

Sale of asset used for scientific research [Sec. 41(3)]

- Without having been used for other purpose:
 - Sale consideration to the extent of cost of such asset shall be taxable as business income in the year of sale.
 - The excess of sale consideration over original cost (or indexed cost of acquisition) is taxable as capital gain u/s 45.
 - This is applicable even if the business is not in existence in that year.
- After being used for other purposes:

Unit 07: Computation of Income under the Head Business & Profession

- Sale consideration shall be subtracted from relevant block of assets.
- It is to be noted that at the time of conversion of scientific research asset into normal business asset, the cost of acquisition shall be taken as nil in the relevant block.

Amortisation of Preliminary Expenses [Sec. 35D & Rule 6AB]

Meaning of Preliminary Expenses:

- Expenses in connection with –
 - Preparation of project report;
 - Preparation of feasibility report;
 - Conducting market survey or any other survey necessary for the business;
 - Engineering services related to the business
- Legal charges for drafting any agreement between the assessee and any other person for any purpose related to the setting up or conduct of business of the assessee.
- Legal charges for drafting & printing of Memorandum of Association & Articles of Association (in case of company-assessee only).
- Registration fees under provisions of the Companies Act, 1956 (in case of company-assessee only).
- Expenses in connection with public issue of shares in or debentures of the company being underwriting commission, brokerage & charges for drafting, typing, printing & advertisement of the prospectus (in case of company-assessee only).
- Any other prescribed expenditure
- Applicable to:
 - An Indian company or a resident non-corporate assessee.
- Conditions
 - Assessee has incurred certain amount as preliminary expense.
 - Purpose of expense
- Where such expense is incurred before commencement of business then expense must be incurred for setting up a new undertaking or business.
- Where such expense is incurred after commencement of business then expense must be incurred in connection with extension of any undertaking or in connection with setting up a new unit.
- Report of a chartered accountant

Total preliminary expense (maximum amount) eligible for deduction

- In case of non-corporate resident assessee
 - 5% of the 'cost of project'.
- In case of Indian company
 - 5% of the 'cost of project' or 'capital employed' whichever is higher

Deduction of expenses incurred in case of amalgamation or demerger [sec. 35dd]

In case of transfer of undertaking under the scheme of amalgamation or demerger, the amalgamated company or resulting company (being Indian company) shall be entitled to claim deduction u/s 35D for the residual period as if the amalgamation or demerger had not taken place [Sec. 35D (5) & (5A)].

Applicable to: An Indian company

Conditions

Assessee has incurred certain expenditure wholly & exclusively for the purpose of amalgamation or demerger.

No deduction has been claimed for such expenses under any other section.

Income Tax Law and Practice

- Quantum of deduction:
 - 1/5th of expenses so incurred for a period of 5 years commencing from the year in which amalgamation or demerger takes places.

Amortisation of expenditure incurred under vrs [sec. 35dda]

- Applicable to All assessee
- Condition:
 - Assessee has incurred any expenditure, by way of compensation to employees in connection with their voluntary retirement.
- Quantum of deduction:
 - 1/5th of expenditure so paid for a period of 5 years commencing from the year in which such expenditure was paid.
- Effect of amalgamation or demerger:
 - the amalgamated company or resulting company (being Indian company) as the case may be, shall be entitled to claim deduction u/s 35DDA for the residual period.

Amortisation of expenditure on prospecting etc. For development of minerals [sec. 35e]

- Applicable to Any Indian company and any other resident assessee.
- Conditions to be satisfied
 - Assessee is engaged in operations relating to prospecting for or extraction or production of mineral specified in Seventh Schedule.
 - Expenditure has been incurred by the assessee on –
 - Prospecting for any mineral specified in Seventh Schedule; or
 - Development of a mine or other natural deposit of any such mineral.

Period during which expenditure is incurred:

- In the previous year in which commercial production commences; and
- At any time during the period of 4 years preceding the year in which commercial production commences.

Following expenditures do not qualify for deduction:

- Expenditure on acquisition of site or any right in or over such site; or
- Expenditure on acquisition of deposits of mineral or any rights in or over such deposits;
- Expenditure of capital nature (being building, plant, machinery or furniture) in respect of which depreciation allowance is admissible u/s 32.
- Any expenditure which is met directly or indirectly by any other person or authority and any sale, salvage, compensation or insurance moneys realized by the assessee in respect of any property or rights brought into existence as a result of the expenditure shall be excluded.

In case of a non-corporate assessee, accounts of the assessee, for the year(s) in which the expenditure is incurred, have been audited by a chartered accountant and the audit report in Form 3AE (electronically) must be uploaded one month prior to the due date of filing of the return of income of the first year in which deduction is claimed.

Quantum of Deduction

- Total eligible expenditure shall be allowed in 10 equal installments from the year of commercial production.
- Treatment of unabsorbed amount: The unabsorbed amount of instalment relating to any previous year can be carried forward and added to the instalment of the succeeding year.

Insurance premium for stocks & stores [sec. 36(1)(i)]

Unit 07: Computation of Income under the Head Business & Profession

- On stocks & stores, used for the purpose of business or profession, is allowable as a deduction in full.

Insurance premium for life of cattle [sec. 36(1)(ia)]

- is allowed as deduction in full.

Insurance premium for health of employees [sec. 36(1)(ib)]

- Insurance on the health of employees under a scheme framed in this behalf by –
 - the General Insurance Corporation of India & approved by the Central Government
 - any other insurer and approved by the Insurance Regulatory and Development Authority shall be allowed as deduction.

Bonus or commission to employees [sec. 36(1)(ii)]

- a. Such amount must have been actually paid before the due date of furnishing return [Sec. 43B]

Interest on borrowed capital [sec. 36(1)(iii)]:

Conditions –

- b. The assessee must have borrowed money.
- c. The money so borrowed must have been used for the purpose of business or profession during the previous year.
- d. The assessee must have incurred interest on the borrowed amount

Other points:

- Interest should be paid to another person.
- Interest paid to a relative, if the interest paid is in excess of market rate then excess portion shall be disallowed.
- Need of such borrowings cannot be challenged by the Assessing Officer
- Interest on share capital is not allowed
- Interest on borrowings made for acquiring & installing assets:
 - Prior to commencement of business: Interest is to be added to actual cost
 - After commencement of business but before asset is put to use of the asset: After asset is put to use Interest is allowed u/s 36(1)(iii)
- If borrowed money is utilized in earning non assessable income, interest on such borrowing shall not be allowed as deduction.
- Interest on money borrowed to pay income tax is not allowed
- Interest paid outside India without deducting tax at source is not allowed.
- Amount borrowed may be applied for the purpose of revenue expenditure or capital expenditure.
- Interest on money borrowed for investing as capital in partnership firm is allowed as deduction. Brokerage & Commission for arranging loan paid to an agent is not allowed under this section but allowed u/s 37(1).
- Other interest: Interest other than interest on borrowed capital e.g. interest on deferred payment for purchased of asset, interest on delayed payment of electricity charges, interest on purchase price of raw-material, etc. shall not be allowed under this section but can be claimed u/s 37(1)

CERTAIN DEDUCTIONS TO BE MADE ONLY ON ACTUAL PAYMENT [SECTION 43B]

Income Tax Law and Practice

- a. Any sum payable by way of tax, duty, cess or fee, by whatever name called, under any law for the time being in force, or
- b. Any sum payable by the assessee as an employer by way of contribution to any provident fund or superannuation fund or gratuity fund or any other fund for the welfare of employees, or
- c. Bonus or Commission for services rendered payable to employees, or
- d. Any sum payable by the assessee as interest on any loan or borrowing from any public financial institution or a State Financial Corporation or a State Industrial Investment Corporation, or
- e. Any sum payable by the assessee as interest on any loan or borrowing from a deposit taking non-banking financial company or systemically important non-deposit taking non-banking financial company, in accordance with the terms and conditions of the agreement governing such loan or borrowing, or
- f. Interest on any loan or advance from a scheduled bank or co-operative bank other than a primary agricultural credit society or a primary co-operative agricultural and rural development bank, in accordance with the terms and conditions of the agreement governing such loan or borrowing, or
- g. Any sum paid by the assessee as an employer in lieu of earned leave of his employee, or
- h. Any sum payable by the assessee to the Indian Railways for use of Railway assets.

INVESTMENT IN NEW PLANT OR MACHINERY IN NOTIFIED BACKWARD AREA [SEC. 32AD]

- Applicable to All Assessees.
- Conditions to be satisfied:
 - Manufacturing unit:
 - Location: notified backward area of Andhra Pradesh or Bihar or Telangana or West Bengal.
 - Acquisition of new assets: during 01-04-2015 to 31-03-2020

“New asset” means any new plant or machinery (other than ship or aircraft) but does not include:

- any plant or machinery which before its installation by the assessee was used either within or outside India by any other person (i.e., second hand);
- any plant or machinery installed in any office premises or any residential accommodation, including accommodation in the nature of a guest house; any office appliances including computers or computer software;
- any vehicle; or
- any plant or machinery, the whole of the actual cost of which is allowed as deduction (whether by way of depreciation or otherwise) in computing the income chargeable under the head “Profits and gains of business or profession” of any previous year.

Quantum of deduction:

- 15% of the actual cost of such new asset installed during the previous year.

Lock-in-period: 5 years

Amalgamation or Demerger or business reorganisation: within a period of 5 years from the date of its installation, the provisions of lock-in-period shall apply to the amalgamated company or the resulting company, as the case may be, as they would have applied to the amalgamating company or the demerged company.

SPECIAL DEDUCTION FOR ASSESSEE ENGAGED IN TEA, COFFEE OR RUBBER GROWING & MANUFACTURING BUSINESS [SEC. 33AB AND RULE 5AC]

Unit 07: Computation of Income under the Head Business & Profession

Applicable to All assessee carrying on business of growing and manufacturing of the followings in India:

- a. Tea;
- b. Coffee; or
- c. Rubber

Conditions to be satisfied

1. Deposit of amount:
2. Time of deposit:
3. Audit of accounts:

Quantum of Deduction:

Minimum of the following –

- a. Amount so deposited (as discussed above); or
- b. 40% of the profit of such business computed under the head “Profits & gains of business or profession” before allowing any deduction u/s 33AB and before adjusting brought forward business loss.

Excess Deposit: not treated as deposit made for the next year(s).

No deduction shall be allowed in respect of any amount, being credited in special account, utilised for the purpose of:

- Purchase of plant or machinery to be installed in any office premises / residential accommodation / accommodation in the nature of guest-house. • Purchase of any office appliances (other than computer)
- Purchase of any plant or machinery, the entire cost of which is allowed as deduction in form of depreciation or otherwise in any one previous year. •
- Purchase of any plant or machinery to be installed in an industrial undertaking for constructing, manufacturing or producing any items specified in Schedule XI of the Act.

Withdrawal from account:

- During continuation of business
- On closure of business:
 - Closure of business: Fully taxable
 - Dissolution of firm: Fully taxable
 - Death of the tax payer: Not taxable
 - Partition of Hindu Undivided Family: Not taxable
 - Liquidation of company: Not taxable
- Restriction on sale of new asset: cannot be sold or transferred within 8 years from the end of the previous year in which it was acquired.
- However, in the following cases, above provision shall not be applicable –
 - Sale or transfer to the Government, local authority, statutory corporation or Government company.
 - Sale or otherwise transfer, in connection with the succession of a firm by a company, provided the following conditions are satisfied –
 - a. All assets & liabilities of firm (immediately before succession) become the assets & liabilities of the company.
 - b. All shareholders of the company were partners of the firm immediately before the succession.
 - c. The scheme continues to apply to the company in the manner applicable to the firm.

Income Tax Law and Practice

- Calculation of taxable income:
 - Tea growing & manufacturing business (Rule 8): 40% of [Income from business - Deduction u/s 33AB]
 - Coffee growing & manufacturing business (Rule 7B): 25% / 40% of [Income from business - Deduction u/s 33AB]
 - Rubber growing & manufacturing business (Rule 7A): 35% of [Income from business - Deduction u/s 33AB]

DISCOUNT ON ISSUE OF ZERO COUPON BONDS (ZCB) [SEC. 36(1)(iia)]

- Discount on issue of Zero Coupon Bonds shall be allowed on pro rata basis having regard to the period of life of such bond.

CONTRIBUTION TOWARDS NOTIFIED PENSION SCHEME U/S 80CCD [SEC. 36(1)(iva)]

- Any sum paid by the assessee, as an employer, by way of contribution towards a pension scheme, as referred to in section 80CCD, on account of an employee is allowed as deduction.
- Maximum Limit: Such contribution should not exceed 10% of the salary of the employee in the previous year.

CONTRIBUTION TOWARDS APPROVED GRAGUITY FUND [SEC. 36(1)(v)]

- Such amount must have been actually paid before the due date of furnishing return [Sec. 43B]

EMPLOYEE'S CONTRIBUTION TOWARDS STAFF WELFARE SCHEME [SEC. 36(1)(va)]

- Any sum received by an employer from his employees as contribution towards -
 - Provident Fund; or
 - Superannuation Fund; or
 - Any other fund set up under the provision of the Employee's State Insurance Act, 1948; or
 - Any other fund for the welfare of such employees -
- is treated as an income of the employer.
- If employees' contribution is not deposited by the employer on or before the due date: Taxable as business income.

ALLOWANCE IN RESPECT OF DEAD OR USELESS ANIMALS [SEC. 36(1)(vi)]

Sec. 36(1)(vi) provides for deduction in respect of animals used for the purpose of business or profession.

- (a) Animals are used for the purpose of business or profession.
- (b) Such animals are not held as stock-in-trade.
- (c) Such animals have died or become permanently useless for such purpose.

Quantum of deduction

- Difference between actual cost of the animals to the assessee and the amounts realised, if any, in respect of carcasses or sale of animals is allowed as deduction.

Bad debts [Section 36(1)(vii) and section 36(2)]

- Debt must be incidental to the business or profession of the assessee
- The debt has been considered as income of the assessee of that previous year or of earlier previous years.
- It must have been written off in the accounts of the assessee.

Bad debts [Section 36(1)(vii) and section 36(2)]

- Business must be carried on during the previous year or any part of the previous year.
- It must be of a revenue nature

Unit 07: Computation of Income under the Head Business & Profession

Recovery of bad debts [Sec. 41(4)] As per sec. 41(4)

- If the amount subsequently recovered on any such debt or part thereof is greater than the difference between the debt or part of debt and the amount so allowed, the excess shall be deemed to be profits and gains of business or profession.

7.5 Meaning of Book profit

Book profit means the net profit as shown in the P & L A/c for the relevant previous year computed in accordance with the provisions for computing income from profits and gains.

Firm's Business Income

In the case of any firm assessable as such or a limited liability partnership (LLP), the following amounts shall not be deducted in computing the business income.

Section 40(b)

- Remuneration to non-working partner
- Remuneration to a working partner not authorized by deed
- Remuneration to a working partner or interest to a partner authorized by deed but relates to an earlier period
- Interest to any partner in excess of 12% p.a
- Remuneration to a working partner in excess of prescribed limits -
- Any remuneration paid to a working partner, authorised by a partnership deed and falling after the date of the deed in excess of the following limits:
 - On the first 3 lakh of book profit or in case of loss 1,50,000 or 90% of book profit, whichever is higher
 - on the balance of book profit 60% of book profit

Book Profit:

- The net profit as shown in the profit and loss account for the relevant previous year computed in accordance with the provisions for computing income from profits and gains [Explanation 3 to section 40(b)].
- The above amount should be increased by the remuneration paid or payable to all the partners of the firm if the same has been deducted while computing the net profit

Illustration

- A firm has paid 7,50,000 as remuneration to its partners for the P.Y.2022-23, in accordance with its partnership deed, and
- It has a book profit of 10 lakh.
- What is the remuneration allowable as a deduction?

Solution

The allowable remuneration calculated as per the limits specified in section 40(b)(v) would be -

- On first 3 lakh of book profit [3,00,000 × 90%]: 2,70,000
- On balance 7 lakh of book profit [7,00,000 × 60%]: 4,20,000
- Total Permissible: 6,90,000

The excess amount of 60,000 (i.e., 7,50,000 - 6,90,000) would be disallowed as per section 40(b)(v).

Illustration

A partnership firm having two partners reports a net profit of 7,00,000 before deduction of the following items:

Income Tax Law and Practice

1. Salary of 20,000 each per month payable to two working partners of the firm (as authorized by the deed of partnership).
2. Depreciation on plant and machinery under section 32 (computed) 1,50,000.
3. Interest on capital at 15% per annum (as per the deed of partnership). The amount of capital eligible for interest is 5,00,000.

Compute:

- a. Book-profit of the firm under section 40(b) of the Income-tax Act, 1961.
- b. Allowable working partner salary for the assessment year 2023-24 as per section 40(b)

Solution

Net Profit (before deduction of depreciation, salary and interest) 7,00,000

- Less:
- Depreciation under section 32 1,50,000
- Less:
- Interest @ 12% of 5,00,000 p.a. 60,000
- Book Profit 4,90,000

In the present case, the net profit given is before deduction of depreciation on plant and machinery, interest on capital of partners, and salary to the working partners. Therefore, the book profit shall be as follows:

- Salary actually paid to working partners = $20,000 \times 2 \times 12 = 4,80,000$.
- As per the provisions of section 40(b)(v), the salary paid to the working partners is allowed subject to the following limits - On the first 3,00,000 of book profit or in case of loss 1,50,000 or 90% of book profit, whichever is more On the balance of book profit 60% of the balance book profit
- Therefore, the maximum allowable working partners' salary for the A.Y. 2023-24, in this case, would be:
- On the first 3,00,000 of book profit : 2,70,000
- [(1,50,000 or 90% of 3,00,000) whichever is more]
- On the balance of book profit : 1,14,000
- [60% of (4,90,000 - 3,00,000)]
- Allowable working partner salary for the assessment year 2023-24 as per section 40(b):
- Maximum allowable partners' salary is 3,84,000
- Hence, allowable working partners' salary for the A.Y.2023-24 as per the provisions of section 40(b)(v) is 3,84,000

Illustration

To Opening Stock	1,20,000	By Sales	2,14,20,000
To Purchases	2,10,00,000	By Profit sale(import licence)	5,000
To Salaries	25,000	By Gift received	24,000
To Legal Expenses	10,000	By Closing Stock	2,00,000
To Bad Debts	5,000		
To Rent	50,000		
To Interest on loan	2,500		

Unit 07: Computation of Income under the Head Business & Profession

To Depreciation	15,000		
To Income tax paid	2,000		
To Outstanding Customs Duty	25,000		
To Advertisement	2,000		
To Legal expenses	12,000		
To URPF Contribution	5,000		
To General expenses	17,500		
To Traveling expenses	1,00,000		
To Net Profit	2,58,000		
	2,16,49,000		2,16,49,000

In computing the income, the following facts are to be taken into consideration:

- Interest on the loan is paid to the brother of Shri Khote for a loan taken for payment of advance income tax.
- During the previous year 2017-18, the assessee had claimed 45,000 as bad debt out of which only 35,000 was allowed. During the previous year, he recovers 25,000.
- Contribution towards unrecognised provident fund was paid within the time.
- Legal expenses include 2,000 paid for preparation of income tax return.
- Stock is undervalued by 10%.
- Gift received was given by a supplier for achieving the target sale.
- Outstanding customs duty has been paid on 31-12-2022.
- During the previous year, he comes to know that his former employee had embezzled cash of 5,000 on 31-3-2021, which was not accounted for.
- Traveling expenses include 50,000 being the cost of a trip to Singapore by an employee for 10 days. However, only 8 days of trip is useful to business and 2 days have been allowed as a holiday to the employee.
- Rent includes expenditure on the extension of a shed on a rented building 26,000. However, such an extension was completed on 1-5-2022 with a total cost of 50,000.
- General expenses include -
 - Salary of 1,200 paid to a domestic servant.
 - Compensation of 2,000 paid for retrenchment of an employee.
- Compute his business income for the A.Y. 2022-23

Solution

Net profit as per Profit and Loss A/c		2,58,000
Add: Expenditure disallowed but debited in P/L A/c		
1. Income tax paid	2,000	
2. Outstanding Customs Duty	25,000	

Income Tax Law and Practice

3. Contribution towards unrecognised provident fund	5,000	
4. Interest on loan	2,500	
5. Expenditure on extension of building shed	26,000	
6. Salary paid to domestic servant	1,200	
		3,19,700
Total Profits after 6 point adjustments		3,19,700
Add: Income taxable but not credited to P/L A/c		
Recovery of bad debts [25,000 - (45,000 - 35,000)]	15,000	
		3,34,700
Total Profits		3,34,700
Less: Expenditure allowed, not debited to P/L A/c		
Embezzlement by employee	5,000	
		3,29,700
Total Profits		3,29,700
Adjustment for valuation of stock		
Add: Under valuation of closing stock	22,222	
Less: Under valuation of opening stock	13,333	8,889
Profits and gains of business or profession		3,38,589

Summary

The provisions for computation of Income from Business or Profession are applicable for Persons who are not in employment and earn income being their own masters. There are many deductions allowed to such persons from their Income but there also many conditions for allow ability of the same. Sections 28 to 44D contain the provisions for computation of Income from Business and Profession. Section 28 defines the scope of income which can be taxed under this head. Sections 29 to 44D specify the method of computation of income under the business or profession. Expenses/allowances expressly allowed by the Act are listed under sections 29 to 37, whereas sections 40, 40A and 43B enumerate those expenses which are expressly disallowed while computing taxable income under this head.

Keywords

- Zero Coupon Bond: As per Sec.2(48) "Zero Coupon Bond" means a bond – - issued by any infrastructure capital company or infrastructure capital fund or public sector company or scheduled bank on or after 1/6/2005; - in respect of which no payment and benefit is received

Unit 07: Computation of Income under the Head Business & Profession

or receivable before maturity or redemption from the issuer; and - which the Central Government may, by notification in the Official Gazette, specify in this behalf.

- Infrastructure capital company [Sec.2(26A)]: means Such company which makes investment by way of acquiring shares or providing long term finance to any enterprise or undertaking wholly engaged in the following business: Business referred u/s 80IA or 80IAB; Any undertaking developing and building a housing project referred u/s 80IB(10); A project for constructing a hotel for not less than 3 star category; Project for constructing a hospital with at least 100 beds for patients.
- Infrastructure capital fund [Sec.2(26B)]: means Such fund operating under a trust deed established to raise money by the trustees for investment by way of acquiring shares or providing long term finance to any enterprise or undertaking wholly engaged in the following business: Business referred u/s 80IA, 80IAB Any undertaking developing and building a housing project referred u/s 80IB(10) A project for constructing a hotel for not less than 3 star category. Project for constructing a hospital with at least 100 beds for patient
- Book Profit: As per Explanation 3 to section 40(b), "book profit" shall mean the net profit as per the profit and loss account for the relevant previous year computed in the manner laid down in Chapter IV-D as increased by the aggregate amount of the remuneration paid or payable to the partners of the firm if the same has been already deducted while computing the net profit.

Self Assessment

1. Expenditure in case of amalgamation or demerger [section 35 dd] is allowed in..... equal annual installments starting from P/Y of amalgamation or demerge
 - A. 5
 - B. 6
 - C. 10
 - D. 15

2. In respect of deductability of repairs and insurance of machinery, plant or furniture used for the purposes of the business or profession, which of the following is untrue -
 - A. the amount paid on account of current repairs thereto ;
 - B. the amount of any premium paid in respect of insurance against risk of damage or destruction thereof.
 - C. In order to avail deduction,it is mandatory that plant,machinery,or furniture must be utilized for the purpose of assessee's business during the previous year.
 - D. It is nessessary that these assets should be used throughout the previous.

3. In respect of EXPENDITURE ON SCIENTIFIC RESEARCH [SECTION 35] which of the following is untrue:
 - A. In-house Scientific Research has to be related to Assessee Business.
 - B. Pre commencement covers 2 years prior to date of commencement of Business.
 - C. Salary of Research Staff is included in Pre commencement covers 3 years prior to date of commencement of Business.
 - D. Deduction for pre commencement expenditure in P/Y of commencement

4. Which of the following is wrong in regard to Calculation of Deduction u/s 35
- A. Revenue expenditure on scientific research is 100% allowed as deduction irrespective of profits.
 - B. Capital expenditure on scientific research are allowed as deduction subject to availability of profit.
 - C. Set off & Carry forward same as unabsorbed depreciation
 - D. Capital expenditure on scientific research are disallowed.
5. Contributions/Donations for Research to Approved Research association/ University /College for scientific research is %allowed wef A/Y 21/22
- A. 100
 - B. 150
 - C. 200
 - D. 300
6. Contributions/Donations for Research to Approved Research association /University, Institution for Social science or statistical research is %allowed wef A/Y 21/22
- A. 100
 - B. 150
 - C. 200
 - D. 300
7. Contributions/Donations for Research to National Laboratory or University or IIT for approved Scientific Research Programme is%allowed wef A/Y 21/22
- A. 100
 - B. 150
 - C. 200
 - D. 300
8. Contributions/Donations for Research to Indian company having main object of scientific research & development & approved by prescribed authority is%allowed wef A/Y 21/22
- A. 100
 - B. 150
 - C. 200
 - D. 300
9. In case of RENT, REPAIRS, TAXES & INSURANCE FOR BUILDINGS [SECTION 30] which of the following statements is untrue?
- A. where the premises are occupied by the assessee as a tenant, the rent paid for such premises is allowed as deduction.
 - B. where the premises are occupied by the assessee otherwise than as a tenant, the amount paid by him on account of current repairs to the premises is allowed as deduction.

Unit 07: Computation of Income under the Head Business & Profession

- C. any sums paid on account of land revenue, local rates or municipal taxes subject to the provision of section 43B is allowed as deduction.
- D. the amount of any premium paid in respect of insurance against risk of damage or destruction of the premises is not allowed as deduction.
10. In case of DEDUCTION FOR BUSINESS OF TEA/COFFEE/RUBBER/EXPLORATION [SECTION 33AB/ ABA] which of the following conditions is untrue?
- A. Deposit with NABARD or Deposit Account under scheme framed by Tea/Coffee/Rubber board with the previous approval of the Central Government within 6 months from end of Previous Year or before due date of furnishing Return, whichever is earlier
- B. Amount withdrawn to be utilised in accordance with scheme specified.
- C. Accounts audited by CA & report attach with Return of Income
- D. Amount withdrawn not utilised for Specified purposes, amount that is not utilised shall be Business Income of the following year.
11. Which of the following mode of payments not allowed u/s 36(1)?
- A. Cash
- B. Cheque
- C. Credit card
- D. Debit Card
12. DEDUCTION OF CAPITAL EXPENDITURE OF SPECIFIED BUSINESS [SECTION 35AD] is % of Capital expenditure incurred wholly and exclusively for the business incurred after commencement including Pre commencement Capital Expenditure.
- A. 50
- B. 100
- C. 150
- D. 200
13. In case of DEDUCTION OF CAPITAL EXPENDITURE OF SPECIFIED BUSINESS [SECTION 35AD], at least.....% of Plant & Machinery should not be Previously used for any purpose:
- A. 50
- B. 80
- C. 150
- D. 200
14. DEDUCTION FOR PROSPECTING MINERALS [SECTION 35E] is allowed in equal expenditure for years starting from previous year of commercial production.
- A. 5
- B. 10
- C. 15
- D. 20

Income Tax Law and Practice

15. Expenses incurred under voluntary retirement scheme [section 35 dda] is allowed in equal annual installments starting from the P/Y in which the amount is actually paid:
- 5
 - 10
 - 15
 - 20

Answers for Self Assessment

- | | | | | |
|-------|-------|-------|-------|-------|
| 1. A | 2. D | 3. B | 4. D | 5. A |
| 6. E | 7. A | 8. E | 9. D | 10. D |
| 11. A | 12. B | 13. B | 14. B | 15. A |

Review Questions

1. What expenses are allowed as deduction from Business or Profession on actual payment basis?
2. What are the cases where capital expenditure is fully allowed as deduction from Business or Profession income?
3. Are expenditures incurred before setting up the business allowed as deduction and if yes what are the limits and conditions?
4. Which taxes are allowed as deduction from Business or Profession Income?
5. What is the importance of method of accounting while computing business or profession income?

**Further Readings**

- https://www.icsi.edu/media/webmodules/16112021_Advance_Tax_Laws.pdf
- Income Tax Law & Practice A.Y 2021-22 by Dr H.C. Mehrotra and Dr. S. P. Goyal. Sahitya Bhawan Publications
- Study Material on Direct Tax Laws and International Taxation by ICAI
- Direct Tax Laws and Practice by Dr. Girish Ahuja & Dr. Ravi Gupta
- <https://cleartax.in/v/it/income-tax-acts-sections/section-28-profits-and-gains-of-business-or-profession-income-tax-act-1961-2019b>

Unit 08: Provisions of Depreciation

CONTENTS

Objectives

Introduction

8.1 Depreciation [Sec. 32]Amended

8.2 Unabsorbed Depreciation [SEC. 32(2)]

8.3 Additional Depreciation [Sec. 32(1)(ia)]

Depreciation Allowable for A.Y.2022-23

8.4 Terminal Depreciation and Balancing Charge

Summary

Keywords

Self Assessment

Answers for Self Assessment

Review Questions

Further Readings

Objectives

After studying this unit, you will be able to:

- Understand the concept and charge of depreciation
- Apply the provisions relating to Depreciation practically.

Introduction

Section 32 of the Income Tax Act of 1961 contains the depreciation allowance clause. A deduction for the real value reduction of a taxpayer's utilised tangible or intangible asset is known as depreciation under the Income Tax Act. Deductions for depreciation are only used for accounting or tax purposes. Definition of Depreciation Depreciation is a tool used to write off the cost of an asset over the course of its usable life. Depreciation must be deducted in some way from an entity's profit and loss accounts, and the Act permits either the Straight-Line approach or the Written Down Value (WDV) method.

8.1 Depreciation [Sec. 32]Amended

Sec. 32 provides for depreciation on

- Tangible assets:
 - Building, Machinery, Plant and Furniture
- Intangible assets
 - Know how, Copyright, Trade Mark, Patent, Licence, Franchise, or any other business or commercial right of the similar nature acquired on or after 1/4/1998 However, it does not include goodwill

Conditions for claiming depreciation

- Condition 1: Asset must be owned by the assessee.

- Condition 2: Asset must be used for the purpose of business or profession during the previous year

Condition 1: Asset must be owned by the assessee

- Beneficial owner
- Co-owner
- Property acquired on hire purchase
- Capital expenditure on a property by the lessee
- Sec. 53A of Transfer of Property Act:

Condition 2: Asset must be used for the purpose of business or profession during the previous year.

- Passive use -vs.- Active use:
- Partly used for business or profession:
- House property let out to tenant for smooth running of the business:

8.2 Unabsorbed Depreciation [SEC. 32(2)]

- Depreciation that could not be fully deducted from profits and gains of the current year of business or profession (due to insufficient profit) is termed as unabsorbed depreciation
- Deducted from income under any other head (except with Casual income and Salaries) of the same assessment year.
- Can be carried forward for an indefinite period and can be set off against any income (except with Casual income and Salaries) of the assessee.

8.3 Additional Depreciation [Sec. 32(1)(iia)]

Applicability: Additional depreciation is applicable on all assessee engaged in the business of manufacture or production of any article or thing or the business of generation, transmission, or distribution of power.

Conditions to be satisfied

1. The assessee must be an industrial undertaking that manufactures or produces any article or thing in the business of generation, transmission, or distribution of power.
2. Assessee acquired and installed after 31st March 2005 a new plant or machinery, other than the following:
 - Ships and air crafts; or
 - Any plant or machinery which was used either within or outside India by any other person before such installation; or
 - Any plant or machinery installed in office premises or any residential accommodation or guest house; or
 - Any office appliances or road transport vehicle; or
 - Any plant or machinery which is allowed for 100% deduction (whether by way of depreciation or otherwise) in the previous year.

Rate of additional depreciation

- Rate of additional depreciation is 20% of the actual cost of such plant or machinery.
- Where, if the asset is acquired and put to use for less than 180 days, then additional depreciation @ 10% (i.e., 50% of 20%) of actual cost shall be allowed in that previous year,

Unit 08: Provisions of Depreciation

and the deduction for the balance 10% shall be allowed in the immediately succeeding previous year

Special Rate of Additional Depreciation in case of notified backward area

Additional depreciation @ 35% (instead of 20%) shall be allowed if the following conditions are satisfied:

1. Assessee sets up an undertaking (or enterprise) for manufacture or production of any article or thing
2. Such undertaking (or enterprise) should be set up on or after 01-04-2015
3. Such undertaking (or enterprise) should be set up in the notified backward area of Andhra Pradesh, Bihar, Telangana, or West Bengal.
4. Assessee acquires and installs any new machinery or plant (other than ships and aircraft or assets referred to above as non-eligible) for such undertaking or enterprise during the period beginning on 01-04-2015 and ending before 01-04-2020 in the said backward area

Extract of depreciation-rate

Residential building other than hotels and boarding	5%
Non residential building, godown, office, factory, etc. including hotels and boarding	10%
Temporary construction	40%
Any furniture including electrical fittings	10%
Ocean going ships, vessels, speed boats	20%
Motor car (including lorries and buses) used for hiring purposes	30%
Motor car, other than used in a business of running them on hire, acquired and put to use between 23-08-2019 and 31-03-2020	30%

Motor buses, motor lorries and motor taxis used in a business of running them on hire, acquired and put to use between 23-08-2019 and 31-03-2020	45%
Computer including computer software Books owned by a professional	40%

Air or water pollution control equipmen	40%
Oil Wells	15%
In general (if nothing is mentioned regarding nature of plant & machinery and including motor car not used for hiring purpose)	15%
Acquired after 31/3/98	25%

Block of Assets [Sec. 2(11)]

- Group of assets of the same nature, in respect of which the same rate of depreciation is charged.

Actual Cost of Assests [SEC. 43(1)]

- In the calculation of actual cost, apart from the cost price of the asset, the following expenditure incurred relating to such asset shall be included:
- Expenses directly related to the acquisition of the Expenses necessary to bring the asset to the site, install it, and make it ready to use.
- Expenses incurred to increase the capacity of the asset or to make it fit prior to its use.

Interest treatment in case of asset acquired out of borrowed fund:

- Before asset is put to use:
- Interest to be added to actual cost
- After asset is put to use:
- Interest is allowed u/s 36(1)(iii)
- Any subsidies received from the Government or any other authority for the purchase of an asset
- Grant or subsidies will be subtracted from the cost of acquisition of such asset.
- Asset acquired from any person using the asset for his business or profession with a view to avoiding tax:
- Actual cost to be determined by the AO with the prior permission of Deputy Commissioner

Reacquisition of transferred asse:

- WDV at the time of first transfer or the price paid for reacquisition, whichever is lower
- Asset acquired by an assessee from another person and given on lease to the same person who had earlier claimed depreciation on such asset:
- WDV of the asset to the transferor

Building used for personal purpose subsequently brought into business:

- Cost of purchase or construction of the building as reduced by the notional depreciation by applying the rate applicable on the date of such conversion

Unit 08: Provisions of Depreciation

Asset, which was acquired outside India, is brought by a non-resident assessee to India and used for his business or profession:

- Actual cost to the assessee, as reduced by an amount equal to the amount of depreciation calculated at the rate in force that would have been allowable had the asset been used in India for the said purposes since the date of its acquisition by the assessee

Any capital asset transferred by a holding company to its 100% subsidiary company or vice versa where the transferee company is an Indian company:

- Actual cost to the transferee company shall be taken to be the same as it would have been if the transferor company had continued to hold the capital asset for the purpose of its business
- Any capital asset transferred by the amalgamating company to the amalgamated company where the amalgamated company is an Indian company
- Actual cost to the amalgamated company shall be taken to be the same as it would have been if the amalgamating company had continued to hold the capital asset for the purpose of its own business

Any capital asset transferred by the demerged company to the resulting company where the resulting company is an Indian company :

- Actual cost to the resulting company shall be taken to be the same as it would have been if the demerged company had continued to hold the capital asset for the purpose of its own business

Capital asset is acquired by the assessee under a scheme for corporatisation of a recognised stock exchange in India

- Actual cost of the asset shall be deemed to be the amount which would have been regarded as actual cost had there been no such corporatisation

Where an assessee was not required to compute his total income under Income tax Act for any previous year(s) preceding the relevant previous year

- Actual cost shall be reduced by the total amount of depreciation on such asset, provided in the books of account (as adjusted by amount attributable to the revaluation of assets) of the assessee in respect of such previous year(s) preceding the relevant previous year
- The actual cost of any capital asset on which deduction is allowable u/s 35AD
- Actual cost of the asset shall be taken as nil

Conversion of inventory into capital asset:

- Where inventory is converted into a capital asset and such converted asset is used for the purposes of business or profession, the actual cost of such asset to the assessee shall be the fair market value which has been taken into account for the purposes of sec. 28(via)

Actual cost in demerger :

- Any capital asset transferred by the demerged company to the resulting company where the resulting company is an Indian company
- Actual cost to the resulting company shall be taken to be the same as it would have been if the demerged company had continued to hold the capital asset for the purpose of its own business

Depreciation in Case of Power Units

At its choice under –

- Written-down value method as followed by all other assesseees (usual); or
- Straight-line method at the prescribed rate in 'Appendix IA' of the Income Tax Rules on the actual cost of the asset
- However, such an option shall be exercised before the due date of furnishing the return of income..

Terminal Depreciation and Balancing Charge

Applicable to: Assessee engaged in generation or generation and distribution of power.

Conditions

1. Assessee must follow the straight-line method of depreciation at specified rates.
2. The asset is sold, discarded, demolished, or destroyed in the previous year (other than the previous year in which it is first brought into use).
3. Loss on the transfer of such asset is treated as terminal depreciation.
4. Terminal depreciation is fully allowed as a deduction as a business loss.

Balancing Charge

- Profit on transfer of such asset to the maximum accumulated depreciation shall be treated as a balancing charge.
- The difference between the sale price and actual cost shall be treated as a capital gain. •
- As per sec. 41(2), balancing charge is fully taxable as business income in the previous year in which such income falls due.

Illustration 1

- Asset acquired F.Y. 2021-22 for the practice of Profession
- Payment by way of account payee cheque.

Sr. No.	Description	Date of acquisition	Date when put to use	Amount
1	Computer including computer software	27 Sept., 21	1 Oct., 21	70,000
2	Computer UPS	2 Oct., 21	8 Oct., 21	17,000
3	Computer printer	1 Oct., 21	1 Oct., 21	25,000
4	Books (other than annual publications are of 12,000)	1 Apr., 21	1 Apr., 21	26,000
5	Office furniture (Acquired from a practicing C.A.)	1 Apr., 21	1 Apr., 21	6,00,000
6	Laptop	26 Sep., 21	8 Oct., 21	86,000

Solution

Block of Assets	
Block 1: Furniture - [Rate of depreciation - 10%]	
Put to use for more than 180 days [6,00,000@10%]	60,000

Unit 08: Provisions of Depreciation

Block 2: Plant [Rate of depreciation- 40%]	
(a) Computer including computer software (put to use for more than 180 days) [70,000 @ 40%]	28,000
(b) Computer UPS (put to use for less than 180 days) [1700@ 20%]	3,400
[See note below]	
(c) Computer Printer (put to use for more than 180 days) [25,000 @ 40%]	10,000
(d) Laptop (put to use for less than 180 days) [86,000 @ 20%]	17,200
[See note below]	
(e) Books (being annual publications or other than annual publications) (Put to use for more than 180 days) [26,000 @ 40%]	10,400
	69,000

Illustration 2

- Mr. G,
- Business of Manufacturing
- Started business on: 1.1.2021.
- unit was set up on: 1.5.2021.
- Operations commenced on: 1.6.2021.
- The total cost of the plant and machinery installed: 120 crores.
 - Included in the above second-hand plant and machinery : 20 crore
 - Included in the above new plant and machinery for scientific research: 15 crores.
- Payment by way of account payee cheque
- 115BAC not opted for.

Solution: Normal Depreciation

Total cost of plant and machinery	120	
Less: Used for Scientific Research	15	
	105	
Normal Depreciation at 15% on 105 crore		15.75

Solution : Additional Depreciation

Additional Depreciation:			
Cost of plant and machinery	120		

Less: Second hand plant and machinery	20		
Plant and machinery used for scientific research, the whole of the 15 actual cost of which is allowable as deduction under section 35(1)(iv) read with section 35(2)(ia)			
		35	
Qualifies for Additional Depreciation:		85	
Additional Depreciation at 20%			17
Depreciation allowable for A.Y.2022-23			32.75

Depreciation Allowable for A.Y.2022-23

Normal Depreciation at 15% on 105 crore		15.75
Additional Depreciation at 20%		17
Depreciation allowable for A.Y.2022-23		32.75

Illustration 3

- Non-Manufacturing Business
- Incurred capital expenditure on purchase of land and building during the period January 2021 to March 2021 exclusively for the above businesses: 50 lakh,
- Capitalized the same in its books of account as on 1st April 2021.
- The cost of land included in the above figures: 30 lakh,
- Incurred capital expenditure on extension/ reconstruction of the building During the P.Y. 2021-22 : 10 lakh

Solution

Depreciation under section 32	In Lakhs
10% of 30 lakh, being (50 lakh – 30 lakh + 10 lakh)	3

Unit 08: Provisions of Depreciation

Illustration 4

- WDV furniture block as on 1/4/2021 80,000.
- (depreciation rate 10%)
- The block consists of two pieces of furniture, X and Y.
- Depreciation u/s 32 for the A.Y. 2022-23?

Case A Furniture X sold for 20,000 on 1/5/2021

W.D.V. as on 1/4/2021	80,000
Add: Purchase	NIL
	80000
Less: Sale Proceeds	20000
	60000
Depreciation	6000
Short term capital gain	Nil
Short term capital Loss	NIL

Case B Furniture X sold for 1,00,000 on 1/1/2022

W.D.V. as on 1/4/2021	80,000
Add: Purchase	NIL
	80000
Less: Sale Proceeds	80000
	Nil
Depreciation	Nil
Short term capital gain	20000
Short term capital Loss	NIL

Sale Proceeds cannot exceed Opening WDV as increased by actual cost of asset acquired during the previous year. Excess, if any, shall be considered as short term capital gain.

Furniture X sold for 1,00,000 and Furniture S purchased for 35,000 as on 1/7/2021

W.D.V. as on 1/4/2021	80,000
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Income Tax Law and Practice

Add: Purchase	35000
	115000
Less: Sale Proceeds	100000
	15000
Depreciation	1500
Short term capital gain	Nil
Short term capital Loss	NIL

Case D Furniture X sold for 10,000 and Furniture S purchased for 40,000 as on 1/7/2021

W.D.V. as on 1/4/2021	80,000
Add: Purchase	40000
	120000
Less: Sale Proceeds	10000
	110000
Depreciation	11000
Short term capital gain	Nil
Short term capital Loss	NIL

Case E Furniture X sold for 10,000 and Furniture S purchased for 40,000 as on 11/11/2021

W.D.V. as on 1/4/2021	80,000
Add: Purchase	40000
	120000
Less: Sale Proceeds	10000
	110000

Unit 08: Provisions of Depreciation

Depreciation (70,000 * 10%) + (40,000 * 10% * 1/2)	9000
Short term capital gain	Nil
Short term capital Loss	NIL

Case G Furniture X and Furniture Y both sold for 10,000 and 35,000 respectively

W.D.V. as on 1/4/2021	80,000
Add: Purchase	-
	80000
Less: Sale Proceeds	45000
Depreciation	nil
Short term capital gain	
Short term capital Loss	35000

Case F Furniture X sold for 2,00,000 and Furniture S purchased for 40,000 as on 11/11/2021

W.D.V. as on 1/4/2021	80,000
Add: Purchase	40000
	120000
Less: Sale Proceeds	120000
Depreciation	NIL
	NIL
Short term capital gain	80,000
Short term capital Loss	NIL

Case H Furniture X and Furniture Y both sold for 10,000 and 35,000 respectively as on 11/11/2021. New Furniture T purchased for 5,000 as on 1/7/2021

Income Tax Law and Practice

W.D.V. as on 1/4/2021	80,000
Add: Purchase	5000
	85000
Less: Sale Proceeds	45000
	40000
Depreciation (40,000 * 10%)	4000
Short term capital gain	NIL
Short term capital Loss	NIL

Case I Furniture Z purchased for 40,000 on 1/7/2021 and the same being put to use on 11/11/2021.

W.D.V. as on 1/4/2021	80,000
Add: Purchase	40000
	120000
Less: Sale Proceeds	NIL
	120000
Depreciation (80,000 * 10%) + (40,000 * 10% * 1/2)	10000
Short term capital gain	NIL
Short term capital Loss	NIL

Case J Furniture Q purchased for 50,000 on 1/7/2021 but put to use on 1/11/2022

W.D.V. as on 1/4/2021	80,000
Add: Purchase	NIL

Unit 08: Provisions of Depreciation

	80000
Less: Sale Proceeds	NIL
	80000
Depreciation (80,000 * 10%)	8000
Short term capital gain	NIL
Short term capital Loss	NIL

Case K Furniture R purchased for 30,000 on 1/7/2020 but put to use on 11/11/2021.

W.D.V. as on 1/4/2021	80,000
Add: Purchase	30,000
	110000
Less: Sale Proceeds	NIL
	110000
Depreciation (110,000 * 10%)	11000
Short term capital gain	NIL
Short term capital Loss	NIL
Though the asset was put to use for less than 180 days but since it was not acquired in the current year hence provision for ½ year depreciation shall not be applicable	
W.D.V. as on 1/4/2021	80,000
Add: Purchase	10,000
	90000

Income Tax Law and Practice

Less: Sale Proceeds	16000
	74000
Depreciation (10,000 * 10% * ½) + (64,000 * 10%)	6900
Short term capital gain	NIL
Short term capital Loss	NIL

Case M Furniture R purchased for 30,000 on 1/7/2021 and sold the same for 40,000 on 11/11/2021.

W.D.V. as on 1/4/2021	80,000
Add: Purchase	30,000
	110000
Less: Sale Proceeds	40000
	70000
Depreciation (70,000 * 10%)	7000
Short term capital gain	NIL
Short term capital Loss	NIL

Case N Sold Furniture X and Y for 95,000 on 1/7/2021 & purchased Furniture R for 30,000 on 11/11/2021

W.D.V. as on 1/4/2021	80,000
Add: Purchase	30,000
	110000
Less: Sale Proceeds	95000
	15000

Unit 08: Provisions of Depreciation

Depreciation (15,000 * 10% * 1/2)	750
Short term capital gain	NIL
Short term capital Loss	NIL

8.4 Terminal Depreciation and Balancing Charge

Applicable to: Assessee engaged in generation or generation and distribution of power.

Conditions

1. Assessee must follow the straight-line method of depreciation at specified rates.
2. The asset is sold, discarded, demolished or destroyed in the previous year (other than the previous year in which it is first brought into use).
 - Loss on the transfer of such asset is treated as terminal depreciation.
 - Terminal depreciation = + ive value of [WDV of assets - (Sale value or Scrap value)]
 - Terminal depreciation is written off in the books of accounts.
 - Terminal depreciation is fully allowed as a deduction as a business loss.

Balancing Charge

- Profit on transfer of such asset to the maximum accumulated depreciation shall be treated as a balancing charge.
- The difference between the sale price and actual cost shall be treated as a capital gain.
- Balancing Charge = - ve value of [WDV of assets - (Sale value + Scrap value)]
- However, balancing charges cannot exceed accumulated depreciation claimed on such asset.
- As per sec. 41(2), balancing charge is fully taxable as business income in the previous year in which such income falls due. The provision holds good even if the business does not exist in that year•

Illustration

- JK Ltd. is a power-generating unit.
- purchased a plant on On 1-4-2019, for: 50,00,000 Depreciation @ 15% on SLM.
- Plant is sold on 21/4/2021 for: 7,50,000

Solution

Computation of Written down value as on 1/4/2021

- Original cost 50,00,000
- Less: Depreciation for the year 2019-20 7,50,000 WDV as on 1/4/2020
42,50,000 Less: Depreciation for the year 2020-21--7,50,000
- WDV as on 1/4/2021 35,00,000

If Sale Proceeds are 7,50,000

Written down value as on 1/4/2021	35,00,000
Less: Sale Proceeds	7,50,000
Balance	27,50,000
Terminal depreciation	27,50,000
Balancing Charge	NIL
STCG	NIL

Illustration

- JK Ltd. is a power-generating unit.
- purchased a plant on On 1-4-2019, for: 50,00,000 Depreciation @ 15% on SLM.
- Plant is sold on 21/4/2021 for: 30,00,000

Sale Proceeds 30,00,000

Solution

Written down value as on 1/4/2021	35,00,000
Less: Sale Proceeds	30,00,000
Balance	5,00,000
Terminal depreciation	5,00,000
Balancing Charge	NIL
STCG	NIL

Illustration

Unit 08: Provisions of Depreciation

- JK Ltd. is a power-generating unit.
- purchased a plant on On 1-4-2019, for: 50,00,000 Depreciation @ 15% on SLM.
- Plant is sold on 21/4/2021 for: 45,00,000

Written down value as on 1/4/2021	35,00,000
Less: Sale Proceeds	45,00,000
Balance	-10,00,000
Terminal depreciation	NIL
Balancing Charge	10,00,000
STCG	NIL

Illustration

- JK Ltd. is a power-generating unit.
- purchased a plant on On 1-4-2019, for: 50,00,000 Depreciation @ 15% on SLM.
- Plant is sold on 21/4/2021 for: 55,00,000

Sale Proceeds 55,00,000

Solution

Written down value as on 1/4/2021	35,00,000
Less: Sale Proceeds	55,00,000
Balance	-20,00,000
Terminal depreciation	NIL
Balancing Charge	15,00,000
STCG	5,00,000

Illustration

- AK Ltd.
- Charging depreciation on straight line method

Income Tax Law and Practice

- Actual cost of the asset: 20,00,000
- Written down value 18,72,300
- Sold the said asset during 2021-22 after 2 years.
- Sales proceeds: 30,000

Solution

- 18,42,300 (being 18,72,300 - 30,000) is treated as terminal depreciation and fully allowed from business income.

Illustration

- AK Ltd.
- Charging depreciation on straight line method
- Actual cost of the asset: 20,00,000
- Written down value 18,72,300
- Sold the said asset during 2021-22 after 2 years.
- Sales proceeds: 18,72,300

Solution: Assessee will cease to get depreciation.

Illustration

- AK Ltd.
- Charging depreciation on straight line method
- Actual cost of the asset: 20,00,000
- Written down value 18,72,300
- Sold the said asset during 2021-22 after 2 years.
- Sales proceeds: 19,80,000

Solution: 1,07,700 (being 19,80,000 - 18,72,300) shall be treated as balancing charge and fully taxable as business income.

Illustration

- AK Ltd.
- Charging depreciation on straight line method
- Actual cost of the asset: 20,00,000
- Written down value 18,72,300
- Sold the said asset during 2021-22 after 2 years.
- Sales proceeds: 19,80,000

Solution:

- 1,07,700 (being 19,80,000 - 18,72,300) shall be treated as balancing charge and fully taxable as business income.

Illustration

- AK Ltd.
- Charging depreciation on straight line method
- Actual cost of the asset: 20,00,000
- Written down value 18,72,300
- Sold the said asset during 2021-22 after 2 years.

Unit 08: Provisions of Depreciation

- Sales proceeds: 21,00,000

Solution:

- 1,27,700 (being 20,00,000 – 18,72,300) shall be treated as balancing charge and fully taxable as business income. And gain of 1 lakh i.e., over and above original cost is treated as short term capital gain.

Illustration

- Dr. K purchased a house property on 1-12-2019 for: 10,00,000.
- Till 1-12-2021, the same was self-occupied as a residence.
- On this date, the building was brought into use for the purpose of his medical profession.

Solution: Notional Depreciation

Rate of depreciation	10%
Cost of building on 1.12.2019	10,00,000
Less: Depreciation	50,000
WDV on 31.3.2020	9,50,000
Less: Depreciation	95,000
WDV on 31.3.2021	8,55,000

Computation of Depreciation U/S 32

- | | |
|-------------------------------------|----------|
| • Cost of building on 1/4/2021 | 8,55,000 |
| • Depreciation for the year 2021-22 | 85,500 |
| • WDV on 01.04.2022 | 7,69,500 |

Illustration

- | | |
|--------------------------------|--------------|
| • A car purchased on: | 10.8.2017 |
| • Purchased for: | 3,25,000 |
| • Purpose: | Personal-use |
| • Brought into the business on | 01.12.2021 |
| • Market value on 01.12.2021 : | 1,50,000. |
| • Rate of depreciation to be | 15%. |

Solution

Cost of the car:	3,25,000
Less: Depreciation:	48,750
Closing W.D.V.	2,76,250

Illustration

W.D.V. of plant and machinery (15%) as on 01-04-2021

- 10,00,000
- Plant D acquired on 10-07-2021 for 5,00,000/-
 - (4,00,000 has been paid through an account payee cheque).
- Put to use on the same day.

Income Tax Law and Practice

- The assessee is engaged in the business of manufacturing.

Solution

- | | |
|--|-----------|
| • WDV as on 01-04-2021 | 10,00,000 |
| • Add: | |
| • Actual cost of Plant D acquired during the year: | 4,00,000 |
| | 14,00,000 |
| • Less: Depreciation for the P.Y. 2021-22 | |
| • [14,00,000 x 15%] | 2,10,000 |
| • Less: Additional Depreciation for the P.Y. 2021-22 | |
| • [4,00,000 x 20%] | 80,000 |
| • WDV on 01-04-2022 | 11,10,000 |

Illustration/M/s KK & Co., a sole proprietary concern, is converted into a company, KK Co. Ltd., with effect from November 29, 2021.

- The written down value of assets as on April 1, 2021, is as follows:
- 10% Building 3,50,000
- 10% Furniture 50,000
- 15% Plant & Machinery 2,00,000
- Further 10% Plant purchases on 15-10-2021 by M/s KK & Co. 1,00,000 .
- Another 15% plant addition after conversion: 50,000

Computation of Depreciation on Assets If There Were No Succession

10% Building

W.D.V. as on 1/4/2021	3,50,000
Add: Purchase during the year	Nil
Less: Sale during the year	Nil
Depreciation	35,000

10% Furniture

W.D.V. as on 1/4/2021	50,000
Add: Purchase during the year	Nil
Less: Sale during the year	Nil
Depreciation	5,000

15% P&M

W.D.V. as on 1/4/2021	200,000
Add: Purchase during the year	1,00,000
Less: Sale during the year	Nil
	3,00,000

Depreciation $[(2,00,000 * 15\%) + (1,00,000 * 15\% * \frac{1}{2})]$ 37,500

Unit 08: Provisions of Depreciation

Calculation of Allowable Depreciation to Sole Proprietary Concern

- Building ($35,000 * 242/365$)=23,205
- Furniture ($5,000 * 242/365$)=3,315
- Plant and Machinery ($30,000 * 242/365$)=19,890
- Plant and Machinery ($7,500 * 45/168$)=2,009

Calculation of Allowable Depreciation to Successor Company

- Building ($35,000 * 123/365$)=11,795
- Furniture ($5,000 * 123/365$)=1,685
- Plant and Machinery ($30,000 * 123/365$)=10,110
- Plant and Machinery ($7,500 * 123/168$)=5,491
- Depreciation in respect of plant purchased after conversion [50% of 15% on 50,000]=3750

Summary

Depreciation is a concept used to write off the cost of an asset over the course of its usable life. An entity using depreciable assets must deduct depreciation from its profits and losses, and the Act permits this to be done either using the Straight-Line technique or the Written Down Value (WDV) approach. The WDV method is frequently used to calculate depreciation. However, there is an option to select the straight-line method if the undertaking is involved in power generation or its generation and distribution. The Act also permits a deduction for additional depreciation in the year of purchase under certain conditions.

Keywords

Residential Building: A building shall be deemed to be a building used mainly for residential purposes, if the built-up floor area thereof used for residential purposes is not less than sixty-six and two-third per cent of its total built-up floor area and shall include any such building in the factory premises.

Depreciation: Depreciation is the methodical distribution of an asset's depreciable value over the course of its useful life. The cost of an asset, or another quantity substituted for cost, less its residual value, is its depreciable amount. The period of time over which an asset is anticipated to be usable by an entity, or the volume of production or similar units anticipated to be received from the asset by the entity, is known as the asset's useful life.

Useful Life: Regardless of the requirements of this Schedule, the useful life or residual value of any specific asset as reported for accounting purposes by a Regulatory Authority established by a Parliamentary Act or by the Central Government shall be applied in calculating the depreciation to be provided for such asset.

Self Assessment

1. What is the rate of depreciation(%) for Residential building other than hotels and boarding?
 - A. 4
 - B. 5
 - C. 7
 - D. 8
2. What is the rate of depreciation (%) for Non residential building, godown, office, factory, etc. including hotels and boarding?
 - A. 10
 - B. 15

- C. 20
 - D. 25
3. What is the rate of depreciation (%) for Temporary construction?
- A. 40
 - B. 50
 - C. 60
 - D. 70
4. What is the rate of depreciation (%) for Any furniture including electrical fittings
- A. 5
 - B. 6
 - C. 7
 - D. 10
5. What is the rate of depreciation (%) for Ocean going ships, vessels, speed boats
- A. 10
 - B. 15
 - C. 20
 - D. 25
6. What is the rate of depreciation (%) for Motor car (including lorries and buses) used for hiring purposes
- A. 10
 - B. 15
 - C. 20
 - D. 30
7. What is the rate of depreciation (%) for Motor car, other than used in a business of running them on hire, acquired and put to use between 23-08-2019 and 31-03-2020
- A. 10
 - B. 15
 - C. 20
 - D. 30
8. What is the rate of depreciation (%) for Motor buses, motor lorries and motor taxis used in a business of running them on hire, acquired and put to use between 23-08-2019 and 31-03-2020
- A. 10
 - B. 15
 - C. 20
 - D. 45
9. What is the rate of depreciation (%) for Computer including computer software Books owned by a professional
- A. 10
 - B. 15

-
- C. 40
D. 45
10. What is the rate of depreciation (%) for Air or water pollution control equipment?
A. 10
B. 15
C. 40
D. 45
11. What is the rate of depreciation (%) for In general (if nothing is mentioned regarding nature of plant & machinery and including motor car not used for hiring purpose)
A. 15
B. 20
C. 25
D. 30
12. What is the rate of depreciation (%) for Intangible assets Acquired after 31/3/98?
A. 25
B. 30
C. 35
D. 40
13. Which of the following is wrong about actual cost determination?
A. In case of Reacquisition of transferred asset: actual cost is WDV at the time of first transfer or the price paid for reacquisition, whichever is lower
B. In case of Asset acquired from any person using the asset for his business or profession with a view to avoiding tax: Actual cost to be determined by the AO with the prior permission of Deputy Commissioner
C. In case of Any subsidies received from the Government or any other authority for the purchase of an asset: Grant or subsidies will be subtracted from the cost of acquisition of such asset.
D. In case of Building used for personal purpose subsequently brought into business: Cost of purchase or construction of the building as increased by the notional depreciation by applying the rate applicable on the date of such conversion
14. Which of the following is wrong about Terminal depreciation?
A. Assessee must follow the straight-line method of depreciation at specified rates.
B. The asset is sold, discarded, demolished, or destroyed in the previous year (other than the previous year in which it is first brought into use).
C. Loss on the transfer of such asset is treated as terminal depreciation.
D. Terminal depreciation is not allowed as a deduction as a business loss.
15. Which of the following is wrong about Balancing Charge?
A. Profit on transfer of such asset to the maximum accumulated depreciation shall be treated as a balancing charge.
B. The difference between the sale price and actual cost shall be treated as a capital gain. •

- C. As per sec. 41(2), balancing charge is fully taxable as business income in the previous year in which such income falls due.
- D. As per sec. 41(2), balancing charge is nontaxable as business income in the previous year in which such income falls due.

Answers for Self Assessment

- | | | | | |
|-------|-------|-------|-------|-------|
| 1. B | 2. A | 3. A | 4. D | 5. C |
| 6. D | 7. D | 8. D | 9. C | 10. C |
| 11. A | 12. A | 13. D | 14. D | 15. D |

Review Questions

1. What prerequisites must be met in order to deduct depreciation from income?
2. Why is depreciation not deductible from taxes?
3. What conditions must be met in order for the additional depreciation to be permitted, as well as what percentage there is to be allowed.
4. Consider writing about terminal depreciation.
5. Make a note on balance charges.



Further Readings

- https://www.icsi.edu/media/webmodules/16112021_Advance_Tax_Laws.pdf
- Income Tax Law & Practice A.Y 2021-22 by Dr H.C. Mehrotra and Dr. S. P. Goyal. Sahitya Bhawan Publications
- Study Material on Direct Tax Laws and International Taxation by ICAI
- Direct Tax Laws and Practice by Dr. Girish Ahuja & Dr. Ravi Gupta
- <https://www.incometaxindia.gov.in/Charts%20%20Tables/Deductions.htm>

Unit 09: Computation of Income from Other Sources

CONTENTS

Objectives

Introduction

9.1 Income Under Head Income From Other Sources

9.2 Agricultural income [Section 10(1)]

Summary

Self Assessment

Answers for Self Assessment

Review Questions

Further Readings

Objectives

After studying this unit, you will be able to:

- Identify the income that falls under the heading "Income from Other Sources" and is subject to tax;
- determine whether transactions involving the receipt of money or property without consideration or for insufficient consideration are subject to taxation under this head;
- be aware of the allowable deductions when calculating income under this heading
- compute the income chargeable to tax under head "Income from other sources"
- understand the definition and range of agricultural income and use these concepts to determine whether a certain income qualifies as agricultural revenue for the sake of section 10(1) exemption;

Introduction

Income from Other Sources is one of the five heads of income subject to taxation under the Income Tax Act, 1961. Any income that is not covered in the other remaining four heads of income is taxed under income from other sources. It is referred to as residuary head of income. Incomes excluded from salary, house property, business & profession (PGBP) or capital gains are covered in Income from Other Sources, barring incomes that are exempt under the Income Tax Act. Under Section 56 of the Act, the following three conditions must be satisfied for a receipt of earning to come under the 'income from other sources' head -1. You have an income.2. Such income is not tax-exempt under any other Sections of the Income Tax Act 1961 3. Such income cannot be categorized as salary, profits, and gains from business or profession, income from house property, or capital gains

9.1 Income Under Head Income From Other Sources

Any income which is not chargeable to tax under any other heads of income and which is not to be excluded from the total income shall be chargeable to tax as residuary income under the head "Income from Other Sources."

Nature of Income Taxable As Residuary Income

- Dividend Income

- Income by way of winnings from lotteries, crossword puzzles, races including horse races, card games, gambling, or betting of any form or nature whatsoever.
- Any sum received by an employer from his employees as a contribution towards PF/ESI/ Superannuation Fund etc.
- If same is not deposited in the relevant fund and it is not taxable under the head 'Profits and Gains from Business or Profession.'
- Interest on securities, if not taxable under the head 'Profits and Gains of Business or Profession.'
- Income from machinery, plant, or furniture belonging to taxpayer and let on hire, if income is not chargeable to tax under the head 'Profits and Gains of Business or Profession'
- Composite rental income from letting of plant, machinery, or furniture with buildings, where such letting is inseparable and such income is not taxable under the head 'Profits and Gains of Business or Profession'
- Any sum received under Keyman Insurance Policy (including bonus), if not taxable under the head 'Profits and Gains of Business or Profession' or under the head 'Salaries'
- If shares in a closely held company are received by a firm or another closely held company from any person without consideration or for inadequate consideration, the aggregate fair market value of such shares as reduced by the consideration paid, if any, shall be chargeable to tax.

Note:

Nothing would be chargeable to tax if the taxable amount doesn't exceed Rs. 50,000.

- If a closely held public company receives any consideration for the issue of shares that exceed the fair market value of such shares, the aggregate consideration received for such shares as reduced by its fair market value shall be chargeable to tax.

Note: This provision is not applicable in the following cases:

- Where the consideration for issue of shares is received by a venture capital undertaking from a venture capital company or venture capital fund or a specified fund.
- Where the consideration for issue of shares is received by company from class or classes of person as notified by the Government.
- In this regard, the Government has provided that section 56(2)(viib) shall not apply where consideration is received by a start-up company in respect of shares issued to a resident person.
- However, a start-up company shall fulfil the condition mentioned in the Notification No. 127(E), dated 19-02-2019 issued by the Department for Promotion of Industry and Internal Trade (DPIIT).
- With a view to ensure compliance to the conditions specified in the said notification, the Finance (No. 2) Act, 2019 reiterates that in case of failure to comply with the conditions specified in the notification, the consideration received from issue of shares as exceeding the fair market value of such shares, shall be deemed to be income of the company chargeable to tax for the previous year in which such failure takes place.
- Further, it shall be deemed that the company has misreported the said income and, consequently, a penalty of an amount equal to 200% of tax payable on the underreported income (i.e., difference between issue price and fair market value of shares) shall be levied as per section 270A.
- Any compensation received by a person in connection with the termination of his employment or modification of terms and conditions relating thereto

Unit 09: Computation of Income from Other Sources

- Interest received on compensation or enhanced compensation
- Any sum of money received as an advance or otherwise in the course of negotiations for the transfer of a capital asset shall be charged to tax under this head, if:
 - Such sum is forfeited; and
 - The negotiations do not result in transfer of such capital asset.
- Gifts:
 - Any sum of money or property received by a person from any person (except from relatives or member of HUF or in given circumstances, see note 1) shall be taxable under the head 'Income from other sources':
 - If any sum is received without consideration in excess of Rs. 50,000 during the previous year, the whole amount shall be chargeable to tax;
 - If an immovable property is received without consideration and the stamp duty value exceeds Rs. 50,000, the stamp duty value of such property shall be chargeable to tax;
 - If immovable property is received for consideration which is less than the stamp duty value of property by higher of following amount the difference is chargeable to tax:
 - the amount of Rs. 50,000
 - the amount equal to 10% of consideration.
 - If movable properties is received without consideration and the aggregate fair market value of such properties exceeds Rs. 50,000, the whole of aggregate fair market value of such properties shall be chargeable to tax
 - If movable properties is received for consideration which is less than the aggregate fair market value of properties by an amount exceeding Rs. 50,000, the difference between the aggregate fair market value and the consideration is chargeable to tax.
 - The stamp duty value may be taken as on the date of agreement instead of the date of registration if the date of the agreement fixing the amount of consideration for the transfer of the immovable property and the date of registration is not the same
 - The Assessing Officer may refer the valuation of such property to a Valuation Officer.
 - If such value is less than the stamp duty value, the same would be taken for determining the value of such property, for computation of income under this head in the hands of the buyer.
 - Notes
 - Any sum of money received by an individual, from any person, in respect of any expenditure incurred by him on his medical treatment or treatment of any member of his family in respect of any illness related to COVID-19, shall not be considered as income of such person. (subject to certain conditions).
 - Any sum of money received by a family member of a person who died due to COVID-19, the money so received shall not be considered as income of the family member where such money is received from the employer of a deceased person.
 - Where the money is received from any other person, the exemption amount shall be limited to Rs. 10 lakh in aggregate. (subject to certain conditions)
 - Summary of Gifts
 - Money:
 - The whole amount if the same exceeds 50,000.

Movable property:

- Without consideration:
The aggregate fair market value of the property, if it exceeds 50,000.

- Inadequate consideration:

The difference between the aggregate fair market value and the consideration, if such difference exceeds 50,000

Immovable property

- Without consideration:

The stamp value of the property, if it exceeds 50,000

- Inadequate consideration:

The difference between the stamp duty value and the consideration, if such difference is more than the higher of 50,000 and 10% of the consideration.

The difference between the stamp duty value and the consideration, if such difference is more than the higher of 50,000 and 20% of consideration, in case the immovable property is a residential unit which is held as stock-in-trade by the seller and the transfer is during the period between 12.11.2020 and 30.6.2021 by way of first time allotment to the buyer and the consideration for transfer ≤ 2 crores

However, any sum of money or value of property received, in the following circumstances would be outside the ambit of section 56(2)(x) – from any relative; or

- On the occasion of the marriage of the individual;
- Under a will or by way of inheritance; or
- In contemplation of death of the payer or donor, as the case may be; or from any local authority; or
- From any fund or foundation or university or other educational institution or hospital or other medical institution or any trust or institution; or
- From or by any trust or institution registered; or
- By any fund or trust or institution or any university or other educational institution or any hospital or other medical institution. by way of transaction not regarded as transfer⁷ under section 47(i)/(iv)/(v)/(vi)/(vib)/(vid)/(vii).
- From an individual by a trust created or established solely for the benefit of relative of the individual.
- From such class of persons and subject to such conditions, as may be prescribed

Definition of Relative

- In case of an individual –

- spouse of the individual;
- brother or sister of the individual;
- brother or sister of the spouse of the individual;
- brother or sister of either of the parents of the individual;
- any lineal ascendant or descendant of the individual;
- any lineal ascendant or descendant of the spouse of the individual;
- spouse of any of the persons referred in (i) to (vi) above.

- In case of Hindu Undivided Family, any member thereof

Dividend Income

DIVIDEND [SEC. 2(22)]

- Any distribution of accumulated profits (whether capitalized or not), which results in the release of assets of the company [Sec. 2(22)(a)]
- Any distribution of –

Unit 09: Computation of Income from Other Sources

- Debenture, debenture- stock, deposit certificates in any form whether with or without interest to its shareholders (equity as well as preference); and
- Shares to preference shareholders by way of bonus, - to the extent to which company possess accumulated profit (whether capitalized or not) [Sec. 2(22)(b)]
 - c. Distribution on liquidation
 - d. Distribution on reduction of capital
 - e. Advance or loan by a closely held company to its shareholder
 - f. Advance or loan by a closely held company to a specified concern
 - i. If the loan is granted in the ordinary course of its business and the lending of money is a substantial part of the company's business, the loan or advance to a shareholder or the specified concern is not deemed dividend.
 - ii. Where a loan had been treated as a dividend and subsequently, the company declares and distributes a dividend to all its shareholders, including the borrowing shareholder, and the premium so paid is set off by the company against the previous borrowing, the adjusted amount will not be again treated as a dividend
 - iii. Any payment made by a company on the purchase of its own shares from a shareholder in accordance with the provisions of section 77A of the Companies Act, 1956
 - iv. Any distribution of shares on demerger by the resulting companies to the shareholders of the demerged company (whether or not there is a reduction of capital in the demerged company).

Meaning of "Accumulated Profits"

- Accumulated profits in point (a), (b), (d) and (e) above include all profits of the company up to the date of distribution or payment of dividend.
- Accumulated profits in point (c) include all profits of the company up to the date of liquidation, whether capitalized or not.
- But where liquidation is consequent to the compulsory acquisition of an undertaking by the Government or by any corporation owned or controlled by the Government, the accumulated profits do not include any profits of the company prior to the 3 successive previous years immediately preceding the previous year in which such acquisition took place.
- In the case of an amalgamated company, the accumulated profits, whether capitalized or not, of the amalgamating company on the date of amalgamation shall be included in the accumulated profits, whether capitalized or not or loss, as the case may be, of the amalgamated company

Basis of Charge Of Dividend

- Any income by way of dividends received from a company, whether domestic or foreign, is taxable in the hands of a resident shareholder at normal tax rates.
 - Casual Income: Winning From Lotteries, Crossword Puzzles, Etc. [SEC. 56(2)(ib)]
 - Lotteries;
 - Crossword puzzles;
 - Races including horse races;
 - Gambling and betting of any nature or form; or
 - Card games, game show or entertainment program on television or electronic mode and any other game of any sort,

Tax Treatment

- Exemption/deduction [Sec. 58(4)]

- Tax rate [Sec. 115BB]
- Method of grossing up of income / Conversion of income received into gross income in case of casual income
- Tax deducted at source
- Procedure Of Grossing Up, In Case Of Resident Individual Or HUF, Are As Follow
 - Gross Lottery Income = Lottery Income Received/ 70%

Interest Received On Compensation/ Enhanced Compensation

Interest received on compensation/ enhanced compensation deemed to be income in the year of receipt and taxable under the head "Income from Other Sources" [Sections 56(2)(viii)]

- i. As per section 145(1), income chargeable under the head "Profits and gains of business or profession" or "Income from other sources", shall be computed in accordance with either cash or mercantile system of accounting regularly employed by the assessee.
- ii. Section 145B(1) provides that notwithstanding anything contained in section 145(1), the interest received by an assessee compensation or on enhanced compensation shall be deemed to be his income for the year in which it is received, irrespective of the method of accounting followed by the assessee.
- iii. Section 56(2)(viii) provides that income by way of interest received on compensation or on enhanced compensation referred to in section 145B(1) shall be assessed as "Income from other sources" in the year in which it is received.

Deductions Allowable [section 57]

- Dividend income: Interest expenditure (maximum of 20% of such income)
- Interest on securities:
 - Commission or remuneration to a banker or any other person for the purpose of realising such interest on behalf of the assessee.
- Recovery from employees as a contribution to any provident fund etc. in terms of section 2(24)(x):
 - To the extent the contribution is remitted before the due date under the respective Acts.
- Income from letting on hire of machinery, plant and furniture, with or without building:
 - the amount paid on account of any current repairs to the machinery, plant, furniture or building.
 - the amount of any premium paid in respect of insurance against risk of damage or destruction of the machinery or plant, furniture or building.
 - the normal depreciation allowance in respect of the machinery, plant or furniture, due thereon.
- Income in the nature of family pension:
 - A deduction of a sum equal to 33-1/3 per cent of such income or ` 15,000, whichever is less, is allowable.
- Any other expenditure not being in the nature of capital expenditure:
 - Deduction allowed if laid out or expended wholly and exclusively for the purpose of making or earning such income.
 - In case of income by way of interest on compensation/ enhanced compensation received chargeable to tax under section 56(2)(viii): Deduction of 50% of such income

Deductions not allowable [section 58]

1. In the case of any assessee:
 - i. any personal expense of the assessee;

- ii. any interest chargeable to tax under the Act which is payable outside India on which tax has not been paid or deducted at source.
 - iii. any payment chargeable to tax under the head "Salaries", if it is payable outside India unless tax has been paid thereon or deducted at source.
 - iv. Any expenditure in respect of which a payment is made to a related person:
2. Considered excessive or unreasonable by the Assessing Officer, having regard to the FMV.
 - i. Disallowance of payment or aggregate of payments exceeding 10,000 made to a person during a day otherwise than by account payee cheque or draft or ECS through a bank account or through such other prescribed electronic mode such as credit card, debit card, net banking, IMPS, UPI, RTGS, NEFT, and BHIM Aadhar Pay covered by section 40A will be applicable to the computation of income under the head 'Income from other sources' as well.
 - ii. Disallowance of 30% of expenditure: in respect of a sum which is payable to a resident and on which tax is deductible at source, if such tax has not been deducted or such tax after deduction has not been paid on or before the due date of return specified in section 139(1).
 - iii. Expenditure incurred in connection with casual income:
 3. No deduction

Illustration 1

- R
- Resident,
- holding 29% of equity shares in a company,
- took a loan of 6,00,000 from the same company.
- On the date of granting the loan, the company had accumulated profit of 3,00,000.
- The company is a manufacturing company.
- How is the loan treated, if the company is a company in which the public are substantially interested?
- How is the loan treated, if the lending company is a private limited company

Solution

- A. The loan would not be taxable as deemed dividend.
- B. Provisions of section 2(22)(e) would be attracted upto accumulated profit of 3,00,000.

Illustration 2

- Mr. A, a dealer in shares,
- Received the following without consideration during the P.Y. 2021-22 from his friend Mr. B, -
 1. Cash gift of 85,000

Occasion: BIRTHDAY, 15th June 2021.
 2. Movable assets,

FMV: 60,000, on his marriage anniversary, 21st June 2021.
 3. A plot of land at Ambala on 1st Aug 2021,

Stamp value: 5 lakh on that date.

Mr. B purchased the land in April 2009.

Mr. A purchased from his friend Mr. C, who is also a dealer in shares,

- 1000 shares of X Ltd. @ 400 each on 19th June, 2021,
- the fair market value of which was 600 each on that date.

- Mr. A sold these shares in the course of his business on 23rd June, 2021.
- On 1st November 2021, Mr. A took possession of the property
- Booked two years back at 20 lakh.
- Stamp duty value as on 1st November 2021: 32 lakh
- Stamp duty value on the date of booking: 23 lakh.
- Paid 1 lakh by account payee cheque as a down payment on the date of booking.
- On 1st March 2022, Ambala Plot sold for 7 lakh.
- Compute the income of Mr. A chargeable under the head "Income from other sources" and "Capital Gains" for A.Y. 2022-23.

Solution

Nature of sum received	Taxable
Cash gift	85,000
Movable Asset	60,000
Stamp value of Ambala plot	5,00,000
Sold shares represent the stock-in-trade of Mr. A.	Not Taxable
Difference between Consideration and stamp duty value of property on the date of booking(23-20)	3,00,000
Income from Other Sources	9,45,000

Computation of "Capital Gains" of Mr. A for the A.Y.2022-23

Particulars	
Sale Consideration	7,00,000
Less: Cost of acquisition	5,00,000
Short-term capital gains	2,00,000

Illustration 3

- HUF received 95,000 in cash from a niece of Karta.
- Answer: Taxable 95,000

Illustration 4

- Nitisha, a member of her father's HUF, transferred a house property to the HUF without consideration. The stamp duty value of the house property is ₹ 9,00,000
- Answer: Not Taxable

Illustration 5

Occasion: marriage anniversary

- Gifts from friend:

- ii. 100 shares of A Ltd.
- iii. FMV: 100 per share.
- iv. Gifts from Nephew:
- v. Jewelry
- vi. FMV: 45,000

Illustration 6

- HUF gifted a car to son of the Karta.
- FMV of the car is 5,25,000.

Answer: Non- taxable

Illustration 7

- Mr. H, a property dealer,
- Sold a building in the course of his business to his friend R, who is a dealer in automobile spare parts, on 1.1.2022: 90 lakh
- stamp duty value on 1.1.2022 : 150 lakh.
- Agreement entered into : 1.9.2021
- Stamp duty value on date of Agreement was: 140 lakh.
- Down payment received : 15 lakh by a crossed cheque on the date of agreement.
- Mr. H had purchased the building for 75 lakh on 12th July, 2020.

Solution

Stamp duty value of property on the date of registration:	15lakh
Actual consideration:	90lakh
Taxable under section 56(2)(x):	60 lakh

Illustration 8 (sub letting)

- Rent on sub-letting of house property 20,000
- Less: Rent paid to original owner 12,000
- Income from other sources 8,000

Illustration 9

- S died on 31st July 2021 while being in Central Government service.
- Mrs. S is paid a family pension of 10,000 p.m. and A dearness allowance of 40% thereof.

Solution

• Family pension:	1,12,000
• [(10,000 + 4,000) x 8]	
• [From 01-08-2021 to 31-03-2022]:	
• Less: Standard deduction	15,000
a) 1/3rd of the pension	37,333
b) Statutory limit	15,000
• Total Income	90,000(Taxable)

Illustration 10

- Interest on enhanced compensation received during the previous year 2021-22 is 6,00,000.
- Out of this interest,
- 2,50,000 relates to the previous year, 2017-18,
- 1,65,000 relates to the previous year 2018-19 and

- 1,85,000 relates to the previous year, 2019-20.
- Discuss the tax implication, if any, of such interest income for A.Y.2022-23.

Solution

Particulars	
Interest on enhanced compensation taxable u/s 56(2)(viii)	6,00,000
Less: Deduction under section 57(iv) @50%	300,000
Interest chargeable under the head "Income from other sources"	3,00,000

Illustration 11: Cash Gifts

(a) Mr. A received cash gift of 1,50,000 from his friend Mr. Las on 10-10-2021

- Solution:
- 1,50,000 shall be considered as income of Mr. A for A.Y. 2022-23

(b) As on 12-11-2021, Mr. A received a cash gift of 50,000 each from his 3 friends

- (one of them is a non-resident)
- Solution: Since the aggregate amount of gift exceeds 50,000, hence, the entire amount of gift, i.e., 1,50,000, shall be considered as income of Mr. A for A.Y. 2022-23

(c) Gift of immovable property

As on 10-01-2022,

- Mr. P received a piece of land from his friend Mr. R without any consideration.
- Stamp duty value: 1,50,000
- land was acquired by R in 2001-02 for 10,000.

on 03-06-2023

- Sold such land for: 2,00,000
- stamp duty value as on date of sale: 2,00,000

Solution

A.Y. 2022-23.

- 150,000 shall be considered as income of Mr. P
u/s 56(2)(x)

A.Y. 2024-25

Sale Consideration: 2,00,000

Less: Cost of acquisition 150,000

Short term capital gain# 1,25,000

Illustration 12

Share Premium in Excess of Fair Market Value [Sec. 56(2)(viib)]

Case 1:

- Shares Issued by P Ltd to Mr. A
- FV: 10
- FMV: 12
- IP: 11
- Solution: Sec. 56(2)(viib) is not applicable

Case 2:

- Shares Issued by P Ltd to Mr. A
- FV: 10
- FMV: 5
- IP: 10
- Solution: Sec. 56(2)(viib) is not applicable

Case 3:

- Shares Issued by P Ltd to Mr. A
- FV: 10
- FMV: 12
- IP: 9
- Solution: Sec. 56(2)(viib) is not applicable

Case 4:

- Shares Issued by P Ltd to Mr. A
- FV: 10
- FMV: 15
- IP: 20
- Solution: Sec. 56(2)(viib) - 5/- per share shall be considered as income in hands of S (P) Ltd. u/s 56(2) (viib)

Case 5:

- Shares Issued by P Ltd to Mr. A (NRI)
- FV: 10
- FMV: 16
- IP: 25
- Solution: Sec. 56(2)(viib) is not applicable

Case 6:

- Shares Issued by P Ltd to Mr. A (NRI at the time of issue of shares. However, later on during the P.Y. he became resident)
- FV: 10
- FMV: 20
- IP: 35
- Solution: 15/- per share shall be considered as income in hands of U (P) Ltd. u/s 56(2) (viib)

Example

- Rent: 20,000 (18,000 for house and 2,000 for AC)
- 18,000 'Income from house property'
- 2,000 'Income from other sources'

Example on Income from Letting of building & machinery

- | | |
|--|----------|
| • Letting of building & machinery under a composite lease: | 1,50,000 |
| • Less: Expenses paid | 10,000 |
| • Collection charges | 1,000 |
| • Repair | 5,000 |
| • Capital repairs | Nil |
| • Depreciation | 4,000 |

- Interest paid outside India without deducting tax on loan taken for construction of building Nil
- Income from Letting of building & machinery 1,40,000

Hotel Business:

Letting of business cannot be segregated from letting up of assets, It is Taxable under PGBP

General Incomes By Virtue of Sec. 56(1).

1. Income from sub-letting of a house property.
2. Interest on bank deposits.
3. Interest on company deposits, interest on loans, etc.
4. Remuneration received from a person other than his employer to evaluate answer scripts. However, if such remuneration is received from the employer, the same will be taxable under the head "Salaries."
5. Rent from a vacant land.
6. Insurance commission.
7. Income from undisclosed sources
8. Income from private tuition.
9. Interest on income tax refund.
10. Taxpoint: Income tax refund itself is not an income.
11. Family pension received by the family members of a deceased employee
12. Dividend received from a co-operative society.
13. Directors' sitting fee for attending Board Meetings. 13. Income from the activity of owning and maintaining race horses.
14. Stipend to the trainee.
15. Interest on employee's contribution towards unrecognized provident funds at the time of payment of lump-sum amount
16. Interest on Securities [Sec. 56(2)(id)]

As per sec. 2(28B), "interest on securities" means -

- a. Interest on any security of the Central Government or a State Government;
- b. Interest on debentures or other securities issued by or on behalf of -
 - i. a local authority; or
 - ii. a company; or
 - iii. a corporation established by a Central, State or Provincial Act

Tax treatment

- When the securities are held as stock-in-trade
 - Taxable under the head 'Profits & gains of business or profession'
- When the securities are held otherwise than as stock-in-trade.
 - Taxable under the head 'Income from other sources.'

Expenditure allowed as deductions by virtue of sec. 57(i) and (iii), from interest income:

- (a) Collection expenditure
- (b) Interest on loan
- (c) Any other expenditure

Illustration 13

- Interest on debenture of A Ltd. received 16,200

Solution:

- Income from other sources:
- 16,200 / 90% 18,000

Illustration 14: Acquisition of Immovable Property At Concessional Amount

- T purchased a piece of land on 10-01-2022,
- Land is purchased from his friend Mr. U against consideration: 30,000
- Stamp duty value is 75,000 •
- Mr. U acquired such land in F.Y. 2006-07: 25,000.
- •Tipu sold such land On 10-04-2023
- Sales consideration: 1,75,000
- Stamp duty value: 1,60,000

Solution

- In hands of Mr. T
 - Provision of sec. 56(2)(x) is not applicable.
 - Cost of acquisition: 30,000
 - Capital Gain: for A.Y. 2024-25
 - Sale Consideration
 - (Higher of 1,75,000 and 1,60,000-Sec.50C)=1,75,000
 - Less: Cost of acquisition=30,000
 - Short term capital gain=1,45,000
- In hands of Mr. U
 - Computation of capital gain for A.Y. 2022-23
 - Consideration (Higher of 75,000 and 30,000 - Sec.50C) 75,000
 - Less: Indexed cost of acquisition
 - [25,000 * 317 / 122] = 64,949
 - Long term capital gain =10,041

9.2 Agricultural income [Section 10(1)]

Section 10(1) provides that agricultural income is not to be included in the assessee's total revenue.

Meaning of Agricultural Income

- Rent or revenue earned from agricultural land situated in India.
- Income derived from agricultural land.
- Income derived from farm building required for agricultural operations.

1. Any Rent or Revenue Derived from a Land, which Is situated In India & is Used for Agricultural Purposes

- Rent or revenue should be derived from the land;
- land has to be situated in India (If agricultural land is situated in a foreign country, the entire income would be taxable); and
- land should be used for agricultural purposes.
- The assessee will not be liable to pay tax on the rent or revenue arising from agricultural land subject to the conditions

1. Income Derived from Agricultural Land.

- Income is derived from agricultural land in the following ways:
- Agriculture basic operations and subsequent operations.

Income Tax Law and Practice

Through the performance of a process by the cultivator or the receiver of rent in kind, the agricultural produce is fit to be taken to the market: The income from the process employed to render the produce fit to be taken to the market

- Through the sale of such agricultural produce:
 - i. Provided it is from the land situated in India and used for agricultural purposes.
 - ii. However, if the produce is subjected to any process other than process ordinarily employed to make the produce fit for the market, the income arising on the sale of such produce would be partly agricultural income and partly non-agricultural income.

Apportionment of Income Between Business Income and Agricultural Income

Crop	Rule	Agricultural Income	Business Income
Growing and Manufacture of Tea	8	60%	40%
Rubber manufacturing business	7A	65%	35%
Coffee grown and cured by seller	7B(1)	75%	25%
Coffee grown, cured, roasted and grounded by the seller in India with or without mixing chicory or other flavouring ingredients	7B(1A)	60%	40%

3. Income Derived from Farm Building Required for Agricultural Operations

The building should be on or in the immediate vicinity of the agricultural land and which the receiver of rent or revenue or the cultivator, because of his connection with the land, requires the building as a house to stay in or as a storehouse or uses it for these kinds of situations.

Additional conditions:

1. The land should either be assessed to land revenue in India or be subject to a local rate assessed and collected by the officers of the Government as such or;
2. Where the land is not so assessed to land revenue in India or is not subject to local rate:-
 1. It should not be situated in any area as comprised within the jurisdiction of a municipality or a cantonment board and which has a population not less than 10,000 or It should not be situated in any area within such distance, measured aerially, in relation to the range of population as shown hereunder -

Aerial distance from municipality*	Population as per last preceding census
Within 2 kms	10,000 to 1,00,000
Within 6 kms	1,00,000 to 10,00,000
Within 8 kms	> Rs. 10,00,000

- If the above condition is not satisfied, the land should not be located within the following region:

Taxation of Agricultural Income

Exemption from income tax

- Partial integration of agricultural income with non-agricultural income when

Unit 09: Computation of Income from Other Sources

- Net agricultural income is more significant than Rs. 5,000 during the year; and non-agricultural income should be higher than the maximum amount not chargeable to tax
- Taxing the non-agricultural income at higher rates of tax.

What Comes Under Agriculture Income?

- Income received from the sale of seeds
- Income received from the growing of flowers and creepers
- Rent received from the use of land for grazing the cattle which are required for agriculture purposes
- Income received from growing of Bamboo

What Does Not Comes Under Agriculture Income?

- Dairy Farming
- Poultry farming
- Livestock Breeding
- Fisheries

How to Evaluate Whether the Particular Agriculture Income is Valid?

- Income should be from an existing piece of land.
- Income should be from a piece of land that is used for agricultural operations.
- Income should stem from products achieved after the cultivation of the land.
- Income can be from land that is not under the assessee's ownership.

Summary

Income from Other Sources includes all types of income that do not fit into one of the other heads. Interest income, dividend income, agricultural income, and all other incomes –aside from salaries, income from house property or capital gains, or income from a business or profession –are included in this area. Certain items of income, such as dividends, Keyman insurance policy winnings, lottery winnings, contributions to provident funds, income from interest on securities, income from hiring machinery, renting out a building with machinery, money gifts, are specifically listed in Section 56(2) as being subject to taxation under the head. Share premiums above fair market value will be considered income and will come in the form of interest on compensation.

Keywords

“Specified fund”: means a fund established or incorporated in India in the form of a trust or a company or a LLP or a body corporate which has been granted a certificate of registration by SEBI as a Category I or Category II Alternative Investment Fund (AIF).

Casual receipt According to the Income-tax Act of 1961, even some irregular revenues are considered income for tax purposes, such as winnings from lotteries and crossword puzzles.

Substantial Interest means: If at any time person entitled to at least 20% income of that concern (20% voting power, in case of company).

Section 2(18): Company in which public are substantially interested (Widely held company): A company is said to be a company in which the public are substantially interested if a. It is owned by Government or Reserve Bank of India or b. Its at least 40% shares are held by the Government or the RBI or c. Nonprofit company or d. company whose principal business is to accept deposits from its members or e. Public company & its equity shares were listed on last day of P/Y on recognized stock exchange A company not covered under above categories is a closely held company

Self Assessment

1. In case of interest received on compensation for compulsory acquisition of capital asset, A deduction of % of such income shall be allowed:
 - A. 50
 - B. 60
 - C. 70
 - D. 80

2. Mr. X got interest in the amount of \$50,000 during P/Y 19/20 as a result of a delay in receiving compensation following the government's forced acquisition of a capital asset. For AY 20-21, ascertain the taxable sum from additional sources.
 - A. 25000
 - B. 50000
 - C. 30000
 - D. 40000

3. Deduction against family pension: 1/3rd of Pension OR /-, whichever is less
 - A. 10000
 - B. 15000
 - C. 20000
 - D. 30000

4. In case of Taxation of gift of Movable property, Without Consideration, Fair market value (FMV) up to is exempt
 - A. 10000
 - B. 20000
 - C. 30000
 - D. 50000

5. In case of Cash Gifts, Sum of money received by ANY PERSON ,Without consideration, In excess of/- in a previous year ,the whole of such sum shall be included in income of receiver under head Other sources:
 - A. 10000
 - B. 20000
 - C. 30000
 - D. 50000

6. Which of the following is wrong in regard to Winnings from Lotteries, Crossword Puzzle, Races including horse races, Card games & other games of any sort or from gambling or betting of any form:
 - A. Deduction u/s Section 80 C to Section 80 U will not be available from such Incomes
 - B. Section 58: No Deduction shall be allowed from such incomes
 - C. Amount to be included in Total Income is Gross amount & not Net amount received after TDS
 - D. Amount to be included in Total Income is Net amount & not Gross amount

7. Mr. X receives the following amount during previous year. calculate his total Income?

Unit 09: Computation of Income from Other Sources

A dividend of ₹ 20,000 from A Ltd, an Indian Company

- A. Exempt
- B. Fully Taxable
- C. Partially taxable
- D. Taxable under Other Sources in hands of Mr.X

8. Mr. X receives the following amount during previous year. calculate his total Income?

A dividend of ₹ 10,000 from Z Ltd, a Foreign Company which has made arrangements for distributing dividends in India

- A. Exempt
- B. Fully Taxable
- C. Partially taxable
- D. Taxable under Other Sources in hands of Mr.X

9. Mr. X receives the following amount during previous year. calculate his total Income?

A dividend of ₹ 15,000 from Z Ltd, a Foreign Company which has not made any arrangements for distributing dividends in India

- A. Exempt
- B. Fully Taxable
- C. Partially taxable
- D. Taxable under Other Sources in hands of Mr.X

10. Mr. X receives the following amount during previous year. calculate his total Income?

Asset of ₹ 18,000 received from B Ltd, an Indian Company

- A. Exempt
- B. Fully Taxable
- C. Partially taxable
- D. Taxable under Other Sources in hands of Mr.X

11. Mr. X receives the following amount during previous year. calculate his total Income?

Debentures worth ₹ 22,000 received from C Ltd, an Indian Company

- A. Exempt
- B. Fully Taxable
- C. Partially taxable
- D. Taxable under Other Sources

12. Mr. X receives the following amount during previous year. calculate his total Income?

A dividend of ₹ 5,000 from a private limited company, an Indian Company

- A. Exempt
- B. Fully Taxable
- C. Partially taxable
- D. Taxable under Other Sources

13. Mr. X receives the following amount during previous year. calculate his total Income?

Income Tax Law and Practice

A Loan of ₹20,000 from a private limited company, an Indian Company in which he holds 15% equity share capital

- A. Exempt
 - B. Fully Taxable
 - C. Partially taxable
 - D. Taxable under Other Sources
14. A company is said to be a company in which the public are substantially interested if following conditions satisfied except:
- A. It is owned by Government or Reserve Bank of India or
 - B. It's atleast 20% shares are held by the Government or the RBI or
 - C. Nonprofit company
 - D. company whose principal business is to accept deposits from its members or
15. Mr. X has let out a car on a rent of ₹1,20,000 during p/y 19/20. The car was purchased on 15/4/2018 for ₹2,00,000. The repair and maintenance expenses incurred on car during previous year 19-20 is ₹30,000. Compute taxable income under other sources for AY 20-21.
- A. 62,250
 - B. 72,250
 - C. 82,250
 - D. 92,250

Answers for Self Assessment

- | | | | | |
|-------|-------|-------|-------|-------|
| 1. A | 2. A | 3. B | 4. D | 5. D |
| 6. D | 7. A | 8. A | 9. D | 10. A |
| 11. A | 12. A | 13. A | 14. B | 15. A |

Review Questions

1. When is income subject to the Other Sources charge?
2. Discuss whether dividends are taxable.
3. What circumstances make the receipt of a gift exempt?
4. What circumstances fall under Section 10(15)'s exemption of Interest?
5. Discuss the Family Pension's taxability.

**Further Readings**

- https://www.icsi.edu/media/webmodules/16112021_Advance_Tax_Laws.pdf
- Income Tax Law & Practice A.Y 2021-22 by Dr H.C. Mehrotra and Dr. S. P. Goyal. Sahitya Bhawan Publications
- Study Material on Direct Tax Laws and International Taxation by ICAI
- Direct Tax Laws and Practice by Dr. Girish Ahuja & Dr. Ravi Gupta
- <https://www.incometaxindia.gov.in/Charts%20%20Tables/Deductions.htm>

Unit 10: Clubbing of Income

CONTENTS

Objectives

Introduction

- 10.1 Income of other Persons Includible in Assesses Total Income
- 10.2 Income Arising to the Spouse from an Asset Transferred without Adequate Consideration [Section 64(1)(iv)]
- 10.3 Asset Transferred Without Adequate Consideration to Son's Wife
- 10.4 Transfer of Assets for the Benefit of Son's Wife [Section 64(1)(viii)]
- 10.5 Clubbing of Minor's Income [Section 64(1A)]
- 10.6 Conversion of Self-Acquired Property into the Property of A Hindu Undivided Family [Section 64(2)]
- 10.7 Income Includes Loss
- 10.8 Distinction between Section 61 And Section 64

Summary

Keywords

Self Assessment

Answers for Self Assessment

Review Questions

Further Readings

Objectives

After studying this unit, you will be able to:

- Determine when clubbing provisions are attracted and use this information to compute the assesses total income.
- Examine the circumstances in which the income of the spouse is combined with the income of the individual and used to compute total income of the individual;
- Examine the circumstances in which the income of the son's wife is included in the hands of the individual and used to compute total income of the individual;
- Identify the type of minor's income that is not subject to clubbing provisions;
- investigate how the minor's income would be included in the hands of the parent as well as compute the amount to be included in hands of the parent;
- examine the occasions whereby HUF income would be included in the hands of a member of the HUF.

Introduction

An assessee is generally taxed on his own income under the Income-tax Act of 1961. However, there are some circumstances in which an assessee must pay tax on the income of another person. Sections 60 to 64 of the Act contain the relevant provisions. These provisions were enacted to mitigate the tendency of taxpayers to dispose of their property or transfer their income in order to avoid or reduce their tax liability. There are various situations where you could need to combine

Income Tax Law and Practice

your income with someone else's money. Hold on if you intend to transfer any of your assets or income to another individual in order to tax-plan and prevent the income from being taxed in your hands. Such transfers can cause clubbing rules under Indian income tax regulations to be attracted. Even sincere gifts given to your family members could result in income tax consequences. You will benefit greatly if you gain some understanding of the clubbing provisions of Indian income tax legislation. So let's get a better understanding of these provisions.

10.1 Income of other Persons Includible in Assesses Total Income

Transfer of Income without Transfer of Asset [Section 60]

Income arising from revocable transfer of assets [Section 61]

Transfer of Income without Transfer of Asset [Section 60]

- If a person transfers the income from an asset without transferring the asset itself, the income is included in the transferor's total income.
- It makes no difference whether the transfer is revocable or irrevocable, or whether it occurred before or after the effective date of this Act.

Income arising from revocable transfer of assets [Section 61]

- All income derived by any person as a result of a revocable transfer of assets is to be included in the transferor's total income.

Meaning of revocable transfer [Section 63]

- A transfer is deemed to be revocable if
 - It contains any provision for the retransfer, directly or indirectly, of the whole or any part of the income or assets to the transferor, or
 - It gives, in any way to the transferor, a right to reassume power, directly or indirectly, over the whole or any part of the income or the assets.

Exception where clubbing provisions are not Attracted even in case of revocable transfer [Section 62]

a. Section 61 will not apply to any income arising to any person if there is -

- i. a transfer by way of trust which is not revocable during the life time of the beneficiary; and
- ii. any other transfer, which is not revocable during the life time of the transferee.

If the transferor receives direct or indirect benefit from such income, such income is to be included in his total income even though the transfer may not be revocable during the life time of the beneficiary or transferee, as the case may be.

As and when the power to revoke the transfer arises, the income arising by virtue of such transfer will be included in the total income of the transferor.



Examples of Revocable Transfers in various situations:

- Case 1 - Where an asset is transferred by the way of trust and it is revocable during the lifetime of the beneficiary.
 - Mr Ram transfers property to a trust for the benefit of Radha and Sharda. However, Ram has the right to revoke the trust while Radha and/or Sharda is alive. This is a revocable transfer, and any income generated from the transferred property is taxable in Ram's hands.
- Case 2 - Where an asset is transferred and it is revocable during the lifetime of transferee.
 - R transfers property to S.

- However, R has a right to revoke such transfer during the lifetime of S.
- This transfer is a revocable transfer and the income generated from such property is taxable in the hands of R.
- Case 3 – Where the transfer contains any provision regarding re-transfer the asset or income to the transferor (directly or indirectly), wholly or partly.
 - R transfers an asset to S.
 - The term of transfer is that on or after 1.04.2008 R can utilize the income of the asset for his benefit.
 - However, he has not exercised this right as yet.
 - On or after 01.04.2008, the income arising from the asset would be taxable in the hands of R, even if he has not exercised the aforesaid right.
- Case 4 – Where the transferor has a right to re-assume the power over the whole or any part of the income or assets (directly or indirectly).
 - R transfers an asset to S.
 - The terms of the transfer are that R can use the asset for the personal benefits of his family members whenever he wants.
 - Till date, he has not exercised this right.
 - Such transfer is a revocable transfer.
 - The entire income arising from the asset would be taxable in the hands of R.
- Income of other Persons Includible in Individuals Total Income
 - Clubbing of income arising to spouse
 - Income by way of remuneration from a concern in which the individual has substantial interest [Section 64(1)(ii)]
 - Remuneration in cash or kind to spouse from a concern in which the individual has substantial interest to be clubbed:
 - In computing the total income of any individual, all such income which arises, directly or indirectly, to the spouse of such individual by way of salary, commission, fees or any other form of remuneration, whether in cash or in kind, from a concern in which such individual has a substantial interest shall be included.
 - Circumstances When an Individual Is Deemed to Have Substantial Interest In A Concern
 1. **Where the concern is a company:**
 - If equity shares carrying 20% or more of voting power are beneficially owned by such person or partly by such person and partly by one or more of his relatives at any time during the P.Y
 2. **In any other case:**
 - If such person is entitled, or such person and one or more his relatives are entitled in the aggregate, to receive 20% or more profit of such concern at any time during the P.Y.
 - **Note:**
 1. The term 'relative' in relation to an individual means the husband, wife, brother or sister or any lineal ascendant or descendant of that individual [Section 2(41)].
 2. Clubbing provisions will not apply where remuneration is received on account of technical or professional qualifications:
 - However, clubbing provisions do not extend where the said individual's spouse has technical or professional credentials and the spouse's income is due entirely to the application of his/her technical or professional knowledge or experience.
 - In such a case, the income derived by such a spouse must be assessed in his or her hands.

3. Both husband and wife have a substantial interest in a concern:

- If both husband and wife have a substantial interest in a business and both receive income from it in the form of salary or other compensation, such income will be includible in the hands of the spouse whose total income, excluding such income, is greater.

10.2 Income Arising to the Spouse from an Asset Transferred without Adequate Consideration [Section 64(1)(iv)]

- Transfer of asset (other than house property):
- Transfer of house property:
- Income from accretion of the transferred asset
- Meaning of adequate consideration
- Transferred asset invested in business

Transfer of Asset (Other Than House Property):

- If an asset (other than house property) is transferred, directly or indirectly, from one spouse to the other without adequate consideration or other than in connection with an agreement to live apart, any income derived by the transferee-spouse from the transferred asset, whether directly or indirectly, is included in the total income of the transferor-spouse.

Transfer of House Property:

- Section 27 contains the provisions for the transfer of house property.
- If an individual transfers a house property to his spouse. Without adequate consideration or other than in connection with a living apart agreement
- The transferor is deemed to be the owner of the house property and its annual value is taxed in his hands.

Income from The Accretion of the Transferred Asset:

- It should be noted that any income from the accretion of the transferred asset is not to be included in the transferor's income.
- Specifically, income from transferred assets must be aggregated.
- However, income earned by investing such income (as a result of a transferred asset) cannot be combined.

Transferred Asset Invested in Business:

- Where assets transferred directly or indirectly by an individual to his spouse are invested in the business by the transferee,
- The transferee's proportionate income from such investment is to be included in the transferor's total income.
- If the investment is in the form of a capital contribution, the transferee's proportionate interest from the firm will be combined with the transferor's income.

Transfer of assets for the benefit of spouse [Section 64(1)(vii)]

- All income derived directly or indirectly from assets transferred directly or indirectly to any person or association of persons by an individual.
- Without adequate consideration is includible in the individual's income.
- To the extent that such income is used by the transferee for the immediate or deferred benefit of the transferor's spouse.

Clubbing of Income arising to Son's Wife

- Income arising to son's wife from the assets transferred without adequate consideration by the father-in-law or mother-in-law [Section 64(1)(vi)]
 - Asset transferred without adequate consideration:
 - Asset transferred invested in the business:
- Transfer of assets for the benefit of son's wife [Section 64(1)(viii)]

10.3 Asset Transferred Without Adequate Consideration to Son's Wife

- When an individual transfers an asset, directly or indirectly, to his or her son's wife,
- Without adequate consideration,
- The income from such asset is included in the transferor's total income.

Asset Transferred Invested in The Business:

- To that end, where assets transferred directly or indirectly by an individual to his or her son's wife.
- Are invested in business by the transferee,
- The proportionate income resulting from such investment is to be included in the transferor's total income.
- If the investment is in the form of a capital contribution, the proportionate interest receivable from the firm will be combined with the transferor's income.

10.4 Transfer of Assets for the Benefit of Son's Wife [Section 64(1)(viii)]

All income derived directly or indirectly from assets transferred directly or indirectly, without adequate consideration, to any person or association of persons by an individual will be included in the individual's total income to the extent such income is used by the transferee for the immediate or deferred benefit of the transferor's son's wife.

10.5 Clubbing of Minor's Income [Section 64(1A)]

- A minor's income must be included in the income of his or her parent.
- But nevertheless, the minor's income from manual labor or any activity requiring his skill, talent, specialized knowledge, or experience will not be included in his parent's income.
- The minor's income will be included in the income of the parent whose total income, excluding the minor's income, is higher.
- If the parents' marriage does not survive, the minor's income is includible in the income of the parent who maintained the minor child in the previous year.
- However, the income of a minor child suffering from any disability of the nature specified in section 80U is not included in the parent's hands but is assessed in the child's hands.
- It should be noted that the clubbing provisions apply even to the income of a minor married daughter.
- If the asset transferred to a minor child (other than a minor married daughter) without consideration or for insufficient consideration is a house property,
 - the transferor-parent is the deemed owner of the house property under section 27(i).
 - As a result, income from house property will be taxable in the hands of the transferor-parent, who is the deemed owner, rather than the minor child.
 - As a result, the clubbing provisions of section 64(1A) would not apply to such income, and the benefit of exemption under section 10(32) (discussed above) would not be available.

Exemption in respect of clubbed income of minor [Section 10(32)]

- Parent shall be entitled to exemption of ₹ 1,500 in respect of each minor child.

10.6 Conversion of Self-Acquired Property into the Property of A Hindu Undivided Family [Section 64(2)]

- Where an individual, who is a member of the HUF, converts at any time after 31-12-1969,
- his individual property into property of the HUF of which he is a member or throws such property into the common stock of the family or otherwise transfers such individual property, directly or indirectly, to the family otherwise than for adequate consideration,
- the income from such property shall continue to be included in the total income of the individual.
- Where the converted property has been partitioned, either by way of total or partial partition,
- the income derived from such converted property as is received by the spouse on partition will be deemed to arise to the spouse from assets transferred indirectly by the individual to the spouse and consequently,
- such income shall also be included in the total income of the individual who effected the conversion of such property.
- Where income from the converted property is included in the total income of an individual under section 64(2), it will be excluded from the total income of the family or, as the case may be, of the spouse of the individual.

10.7 Income Includes Loss

Where the specified income to be included in the total income of the individual is a loss, such loss will be taken into account while computing the total income of the individual.

10.8 Distinction between Section 61 And Section 64

Section 61 applies only to a revocable transfer made by any person.

Section 64 applies to revocable as well as irrevocable transfers made only by individuals.

Illustration: 1

Mr. B grants his wife, Mrs. B, the right to receive rent on his house property without transferring the house itself to her.

Solution

In this case, rent received by Mrs B will be clubbed with Mr B's income.

Illustration: 2

Mr. Vasu has transferred the income from a go down to his son via a duly registered document, but has not transferred the go down itself. Who will be charged with the rental income from the go down?

Solution

Section 60 explicitly says that where income from an asset is transferred without the asset itself being transferred, such income is included in the transferor's total income. As a result, the rental income from the go down will be pooled in the hands of Mr. Vasu.

Illustration: 3

- Mr. B holds shares carrying 25% voting power in JCT Ltd.
- Mrs. B is working in JCT Ltd. at a salary of ₹ 40,000 p.m.

Unit 10: Clubbing of Income

- She is, however, not qualified for the job.
- The other income of Mr. A & Mrs. A is 6,00,000 & 3,00,000, respectively.
- Compute the gross total income of Mr. B and Mrs. B for the A.Y.2022-23, assuming that they do not opt for section 115BAC.

Solution

Computation of Gross total income of Mr. A

Particulars		
Salary received by Mrs. A	4,80,000	
(40,000 × 12)		
Less: Standard deduction under section 16(ia)	50,000	4,30,000
Other Income		6,00,000
Gross total income		10,30,000

Illustration: 4

Will your response change if Mrs. B was qualified for the position?

Solution

Gross total income of Mr. B = 6,00,000 [other income].

Gross total income of Mrs. B

- Salary received by Mrs. B = 4,80,000
- Less standard deduction under section 16(ia) = 50,000,
- Add: Other income = 3,00,000
- GTI Mrs. = 7,30,000

Illustration: 5

- Mr. A owns 40 percent of the voting power in Y (P) Ltd.
- Mrs. A works as an accountant for Y (P) Ltd. and earns a salary (computed) of 4,00,000 despite having no accounting qualifications.
- Mr. A also receives 60,000 in securities interest.
- Mrs. A owns a house, which she rents out. The rent received from tenants is 7,000 per month.
- Calculate Mr. An and Mrs. A s gross total income for the Assessment Year2022-23.

SolutionComputation of Gross total income of Mr. A

Particulars	
Income under the head salary of Mrs. A (Computed)	4,00,000
Income from other sources	
- Interest on securities	60,000
	4,60,000

Income Tax Law and Practice

Computation of Gross total income of Mrs. A		
Particulars	₹	₹
Income from Salary		Nil
[clubbed in the hands of Mr. B]		
Income from house property		
Gross Annual Value [7,000 × 12]	84,000	
Less: Municipal taxes paid	-	
Net Annual Value (NAV)	84,000	
Less: Deductions under section 24		
30% of NAV i.e., 30% of 84,000	25200	
Interest on loan	-	58,800
Gross total income		58,800

Illustration: 6

- Mr. KK transferred debentures of 60,000 carrying 8% interest to his wife.
- The interest income of 4,800 would be clubbed in the hands of Mr. KK.
- However, in case his wife deposited 4,800 in fixed deposits @5%.
- What is the tax treatment of the interest income of 240 arising on FDR?

Solution

The interest income of 240 arising on FDR would not be clubbed in the hands of Mr. KK.

Illustration: 7

	Particulars	₹
(a)	Salary income (computed) of Mrs. B	460000
(b)	Income from profession of Mr. B	780000
(c)	Income of minor son C from company deposit	30000
(d)	Income of minor daughter D from special talent	64000
(e)	Interest from bank received by D on deposit made out of her special talent	6000
(f)	Gift received by D on 30.08.2021 from friend of Mrs. B	5000

Solution

Computation of gross total income of Mr. B for the A.Y. 2022-23		
Particulars	₹	₹
Income from profession		780000

Unit 10: Clubbing of Income

Income of minor son C from company deposit	30000	
Less: Exemption under section 10(32)	1,500	28,500
Income of minor daughter D		
From special talent – not to be clubbed	-	
Interest from bank	6,000	
Gift of 5000 received from a non-relative is not taxable under section 56(2)(x) being less than the aggregate limit of 50,000	Nil	
	6,000	
Less : Exemption under section 10(32)	1,500	4,500
Gross Total Income		8,13,000

Illustration: 8

- Mr. B has three minor children – two twin daughters, aged 11 years, and one son, aged 12 years.
- Income of the twin daughters is 3,000 p.a. each
- Income of the son is 1,000 p.a.
- Mrs. B has transferred her flat to her minor son on 1.8.2021 out of natural love and affection. The flat was let out on the same date and the rental income from the flat is 12,000 p.m.
- Mr. B's total income is higher than Mrs. B's total income.

Solution

Particulars		
Twin minor daughters [3,000 × 2]	6,000	
Less: Exempt under section 10(32) [1,500 × 2]	3,000	3,000
Minor son	1,000	
Less: Exempt under section 10(32)	1,000	Nil
Income to be clubbed in the hands of Mr. A		3,000

Illustration: 9

Mrs. K transferred her immovable property to XYZ Co. Ltd. subject to a condition that out of the rental income, a sum of 66,000 per annum shall be utilized for the benefit of her son's wife.

Mrs. K claims that the amount of 66,000 (utilized by her son's wife) should not be included in her total income as she no longer owned the property.

Examine with reasons whether the contention of Mrs. K is valid in law.

Solution

- The contention of Mrs. K is not valid in law.

Income Tax Law and Practice

- The clubbing provisions under section 64(1)(viii) are attracted in case of transfer of any asset, directly or indirectly, otherwise than for adequate consideration, to any person to the extent to which the income from such asset is for the immediate or deferred benefit of son's wife.
- Such income shall be included in computing the total income of the transferor-individual.
- Therefore, the income of 66,000 meant for the benefit of daughter-in-law is chargeable to tax in the hands of transferor i.e., Mrs. K in this case.

Illustration: 10

- Mr. Vasu started a proprietary business on 01.04.2020 with a capital of 10,00,000. He incurred a loss of 4,00,000 during the year 2020-21.
- To overcome the financial position, his wife Mrs. Vasu, gave a gift of 10,00,000 on 01.04.2021, which was immediately invested in the business by Mr. Vasu.
- He earned a profit of 6,00,000 during the year 2021-22.
- Compute the amount to be clubbed in the hands of Mrs. Vasu for the Assessment Year 2022-23.
- If Mrs. Vasu gave the said amount as loan, what would be the amount to be clubbed?

Solution

Particulars	Mr. Vasu's capital contribution ()	Capital contribution out of gift from Mrs. Vasu ()	Total ()
Capital as on 1.4.2021	6,00,000	10,00,000	16,00,000
	(10,00,000 -4,00,000)		
Profit for P.Y.2021-22 to be apportioned on the basis of capital employed on the first day of the previous year i.e. as on 1.4.2021 (3:5)	225000(6,00,000*3/8)	375000(6,00,000× 5/8)	6,00,000

Summary

According to Sections 60 to 65 of the Income-tax Act, all items of income listed in these sections must be taken into account when calculating a person's total income for assessment purposes. When someone transfers revenue (whether revocable or not) from an asset to another person without also transferring that asset, the income is counted toward the transferor's overall income. Any settlement, trust, covenant, agreement, or arrangement is a "transfer." All income flowing to the transferee from an asset that has been transferred to another person who has the power to revoke the transfer must be included in the transferor's total income. Even if only a portion of the revenue from the transferred asset has been used for the transferor, the income under the revocable transfer of asset must be included in the transferor's income. The income from assets that have been irrevocably transferred for a fixed length of time is not counted in the transferor's income. All money that goes to the minor child (who is not a minor child with a disability of the kind listed in Section 80U) or accrues to him must be included in his parent's income. However, a minor's income from manual labor or from any activity requiring the application of his ability, skill, or specialized knowledge and experience is excluded from his parent's income. If a person's income is subject to this section's [Section 64(1A)] requirements and includes any income of his minor children, such person is eligible for a deduction equal to the lesser of the amount of such income or Rs. 1,500.

Keywords

'**Revocable transfer**' indicates that during the lifetime of the transferee, the asset's transferor assumes the right to repurchase the asset or any income derived from it, in whole or in part. It also

includes transfers that grant the recipient the ability to reacquire the right to receive income from an asset or assets for as long as they live.

Clubbing of income: The situation in which income of other person is included in the income of the taxpayer is called as clubbing of income.

“**Transfer**” includes any settlement, trust, covenant, agreement or arrangement. The transfer also includes a lease for inadequate consideration and the income derived by the lessee from the leased property is included in the income of the lessor.

Converted property Where an individual, being a member of Hindu Undivided Family, transfers his self-acquired property after 31st December, 1969 to the family for the common benefit of the family, or throwing it into the common stock of the family, or transfers it directly or indirectly to the family otherwise than for adequate consideration, such property is known as converted property.

Self Assessment

1. Which of the following is not an example of revocable transfers?
 - A. If there is an express clause of revocation in the instrument of transfer;
 - B. If there is a sale with a condition of re-purchase;
 - C. If the transfer is to a trust and if the transfer can be revoked with the consent of two or more beneficiaries;
 - D. If the trustees are not empowered in sole discretion to revoke the transfer; Answers for Self-Assessment

2. Which of the following statement is wrong about the provisions related to Income to spouse from a concern in which such individual has substantial interest [Section 64(1)(ii)]?
 - A. All such income as arises directly to the spouse of an individual by way of salary, commission, fees or any other remuneration, whether in cash or kind from a concern in which such individual has a substantial interest, shall be included in the income of the individual.
 - B. All such income as arises indirectly to the spouse of an individual by way of salary, commission, fees or any other remuneration, whether in cash or kind from a concern in which such individual has a substantial interest, shall be included in the income of the individual.
 - C. All such income as arises directly or indirectly to the spouse of an individual by way of salary, commission, fees or any other remuneration, whether in cash or kind from a concern in which such individual has a substantial interest, shall be included in the income of the individual.
 - D. All such income as arises directly to the spouse of an individual by way of salary, commission, fees or any other remuneration, whether in cash or kind from a concern in which such individual does not have a substantial interest, shall be included in the income of the individual.

3. Which of the following statement is wrong about the provisions related to Income to spouse from a concern in which such individual has substantial interest [Section 64(1)(ii)]?
 - A. Where both husband and wife have a substantial interest in the concern and both are in receipt of the remuneration in such concern, the remuneration from such concern is to be included in the total income of the husband

- B. Where both husband and wife have a substantial interest in the concern and both are in receipt of the remuneration in such concern, the remuneration from such concern is to be included in the total income of the wife
- C. Where both husband and wife have a substantial interest in the concern and both are in receipt of the remuneration in such concern, the remuneration from such concern is to be included in the total income of the husband or, as the case may be, the wife whose total income excluding the income referred to in that clause i.e. 64(1)(ii) is greater;
- D. Where any such income is once included in the total income of either spouse, any such income arising in any succeeding year shall be included in the total income of the other spouse.
4. Which of the following statement is wrong about the provisions related to Income to spouse from the assets transferred [Section 64(1)(iv)]?
- A. Where any individual transfers directly or indirectly any asset (other than a house property) to the spouse, the income from such asset shall be included in the income of the transferor.
- B. In order to attract the provisions of this section, it is not necessary that the asset must have been transferred by the assessee to his spouse in the same form in which it stands at the time the income arises.
- C. Conversion of assets from one form to another would be totally immaterial
- D. However, it is essential that the transfer must have taken place directly between the spouses.
5. Which of the following statements is wrong?
- A. Suppose, A transfer's certain shares to his wife B. Dividends received on such shares are taxable in the hands of A.
- B. If B sells the shares and makes some capital gains, such gains are also taxable in A's hands.
- C. Now from the dividend money, B purchases some more shares and receives dividends on these new shares, such dividends are also taxable to A.
- D. In the same way, if B receives certain bonus shares on the shares transferred by her husband and later on she receives dividend on such bonus shares, the dividend shall not be included in the income of the transferor because the bonus shares were never transferred by her husband.
6. Which of the following statement is TRUE about the provisions related to transfer for immediate or deferred benefit of son's wife [section 64(1)(viii)]?
- A. Any income arising, directly or indirectly, to any person or association of persons from assets transferred directly or indirectly before June 1, 1973, otherwise than for adequate consideration to the person or association of persons by such individual shall, to the extent to which the income from such assets is for the immediate or deferred benefit of his son's wife be included in computing the total income of such individual
- B. Any income arising, directly or indirectly, to any person or association of persons from assets transferred directly or indirectly after June 1, 1973, for adequate consideration to the person or association of persons by such individual shall, to the extent to which the income from such assets is for the immediate or deferred benefit of his son's wife be included in computing the total income of such individual

- C. Any income arising, directly or indirectly, to any person or association of persons from assets transferred directly or indirectly after June 1, 1973, otherwise than for adequate consideration to the person or association of persons by such individual shall, to the extent to which the income from such assets is not for the immediate or deferred benefit of his son's wife be included in computing the total income of such individual
- D. Any income arising, directly or indirectly, to any person or association of persons from assets transferred directly or indirectly after June 1, 1973, otherwise than for adequate consideration to the person or association of persons by such individual shall, to the extent to which the income from such assets is for the immediate or deferred benefit of his son's wife be included in computing the total income of such individual
7. Which of the following statement is WRONG about the provisions related to clubbing of income of minor child [section 64(1a)]?
- A. All income which arises or accrues to the minor child (not being a minor child suffering from any disability of the nature specified in Section 80U) shall be clubbed in the income of his parent.
- B. However, any income which is derived by the minor from manual work or from any activity involving application of his skill, talent or specialised knowledge and experience will not be included in the income of his parent.
- C. Further, the income of the minor shall be included in the income of that parent whose total income excluding income includible under this subsection is greater, where the marriage of minor's parents subsists, otherwise the income of the minor will be includible in the income of that parent who maintains the minor child in the relevant previous year.
- D. Once the income of the minor is included in the total income of any one parent, clubbing of income of the minor with the same parent will continue in subsequent years also without any exception
8. In case the income of an individual includes any income of his minor child in terms of this section [i.e. Section 64(1A)], such individual shall be entitled to exemption of the amount of such income or Rs. whichever is less.
- A. 500
- B. 1000
- C. 1500
- D. 2000
9. Which of the following statement is WRONG about the provisions related to INCOME FROM THE CONVERTED PROPERTY [SECTION 64(2)]?
- A. The income derived from the converted property or any part thereof, shall be included in the income of the transferor.
- B. The income derived from the converted property or any part thereof, shall be included in the income of the transferee.
- C. For this section "property" includes any interest in property, movable or immovable the proceeds of sale thereof
- D. For this section "property" includes any interest in property, movable or immovable the proceeds of sale thereof and any money or investment for the time being representing the proceeds of sale thereof and where the property is converted into any other property by any method, such other property.

10. Which of the following statement is WRONG about the provisions related to RECOVERY OF TAX under clubbing provisions]?
- A. There is no Dual Liability for Tax.
 - B. The tax on the income of the other person which has been included in the income of the assessee can either be recovered from the assessee or from the other person.
 - C. The liability of other person is limited to the portion of the tax levied on the assessee which is attributable to the income so included.
 - D. The liability of other person arises after the service of a notice of demand by the Assessing Officer in this behalf.
11. Sectiondeals with Clubbing of Income provisions.
- A. 50-55
 - B. 60-65
 - C. 65-70
 - D. 70-75
12. Sectiondeals with Income to spouse through a third person.
- A. Section 64(1)(vii)
 - B. Section 64(1a)
 - C. Section 64(1)(viii)]
 - D. Section64(1)(iv)
13. Sectiondeals with Income to spouse from a concern in which such individual has substantial interest.
- A. Section 64(1)(vii)
 - B. Section 64(1)(ii)
 - C. Section 64(1)(viii)]
 - D. Section64(1)(iv)
14. Sectiondeals with Income to Son's Wife.
- A. Section 64(1)(vi)
 - B. Section 64(1)(ii)
 - C. Section 64(1)(vii)]
 - D. Section64(1)(iv)
15. Whichsection deals with REVOCABLE TRANSFER OF ASSETS.
- A. 61
 - B. 72
 - C. 83
 - D. 93

Answers for Self Assessment

- | | | | | |
|------|------|------|------|-------|
| 1. D | 2. D | 3. D | 4. D | 5. C |
| 6. D | 7. D | 8. C | 9. B | 10. A |

11. B 12. A 13. B 14. A 15. A

Review Questions

1. Argue about the tax treatment of transactions that result in the transfer of income but not the assets that generate the revenue.
2. Argue about how transactions that result in a person giving assets to their spouse, minor children, adult sons, and married daughters are taxed.
3. Describe what is meant by "a revocable transfer" in terms of income tax, and distinguish between revocable and irreversible transfers of assets.
4. Examine the tax repercussions of revocable asset transfers.
5. Examine the tax repercussions of asset transfers that are final.
6. Describe the tax implications of a person creating a trust for (i) himself, (ii) his/her spouse, (iii) their minor children, and (iv) his/her married daughter (v) his daughter-in-law and sisters.



Further Readings

- https://www.icsi.edu/media/webmodules/16112021_Advance_Tax_Laws.pdf
- Income Tax Law & Practice A.Y 2021-22 by Dr H.C. Mehrotra and Dr. S. P. Goyal. Sahitya Bhawan Publications
- Study Material on Direct Tax Laws and International Taxation by ICAI
- Direct Tax Laws and Practice by Dr. Girish Ahuja & Dr. Ravi Gupta
- <https://incometaxindia.gov.in/pages/faqs.aspx>

Unit 11: Set-off Inter Head Provisions, Set-off Intra Head Provisions

CONTENTS

Objectives

Introduction

11.1 Intra-head Adjustment

11.2 Inter-Head Adjustment

11.3 Carry Forward of Loss

Summary

Keywords

Self Assessment

Answers for Self Assessment

Review Questions

Further Readings

Objectives

After studying this unit, you will be able to:

- Understand set off of losses inter-head and intra-head.
- Understand conditions to be satisfied for carry forward and set-off of losses.

Introduction

Specific provisions have been made in the Income-tax Act, 1961 for the set-off and carry forward of losses. In simple words, "Set-off" means adjustment of losses against the profits from another source/head of income in the same assessment year. If losses cannot be set-off in the same year due to inadequacy of eligible profits, then such losses are carried forward to the next assessment year for adjustment against the eligible profits of that year. The maximum period for which different losses can be carried forward for set-off has been provided in the Act. Income from various sources is computed under the five heads of income for the purpose of calculating Gross Total Income (GTI). If all of the sources and heads have positive income (i.e. profit), the GTI can simply be added. However, if one or more sources or heads have negative income (i.e. a loss), that loss must be offset by income from another source or head (s).

11.1 Intra-head Adjustment

Adjustment of Income and loss from all sources covered under one head of Income is called Intra-Head Adjustment [Rules are prescribed in Sec. 70]

- **Example 1:** Loss from one house property can be set off against the income from another house property.
- **Example 2:** Loss from one business, say textiles, can be set off against income from any other business, say printing, in the same year as both these sources of income fall under one head of income. Therefore, the loss in one business may be set-off against the profits from another business in the same year.

- Sec. 70 deals with the set off of loss from one source against income from another source under the same head of income subject to the following exceptions –
 - Long term capital loss can be set off only against long term capital gain [Sec. 70(3)]
- Loss of a speculation business can be set off only against the profits of a speculation business, under the head 'Profits and gains of business or profession'. However, loss from a non-speculative business can also be set off against income from speculation business [Sec. 73(1)]
 - Loss of a specified business covered u/s 35AD D can be set off only against the profits of other specified business.
 - Loss incurred in activity of owning and maintaining race horses can be set off against income from such activity only [Sec. 74A]
 - Loss from a source, income of which is exempt u/s 10
 - No loss can be set off against winning from lotteries, crossword puzzles, races, card games, gambling or betting, etc. [Sec. 58(4) & 115BB].
 - Similarly, set off of losses is not permissible against unexplained income, investment, money, etc. chargeable u/s 68 / 69A / 69B / 69C / 69D [Sec. 115BBE]

11.2 Inter-Head Adjustment

- Adjustment of Income under one head and loss from another head of Income is called inter-head adjustment [Rules are prescribed in Sec. 71]
- Where in respect of any assessment year, the net result of any head of income is a loss, the same can be set off against the income under any other heads for the same assessment year, subject to the following exceptions:
 - Capital gains
 - Loss of a speculation business
 - Loss of a specified business covered u/s 35AD
 - Loss from activity of owning and maintaining race-horses
 - Loss under the head 'Income from house property'
 - Income under the head Salaries:
 - Loss from a source, income of which is exempt u/s 10
- Loss under the head 'Capital gains' cannot be set off against income under any other head.
- However, loss under any other head, e.g. business loss, shall be allowed to be set off against income under the head 'Capital gains'.
- Loss under the head 'Profits and gains of business or profession' due to speculation business cannot be set off against any other income except profits of speculation business.
- However, loss under any other head, e.g. loss from house property, shall be allowed to be set off against income of a speculation business
- Loss of a specified business covered u/s 35AD cannot be set off against income taxable under other head.
- However, loss from other head can be set off against income from specified business.
- Loss under the head 'Income from other sources' due to activity of owning and maintaining race-horses cannot be set off against any other income except profit from activity of owning and maintaining race-horses [Sec. 74A].
- However, loss under any other head, e.g. business loss, shall be allowed to be set off against income from activity of owning and maintaining racehorses.
- Loss in excess of ` 2,00,000 under the head 'Income from house property' cannot be set off with income under other heads of income

Unit 11: Set-off Inter Head Provisions, Set-off Intra Head Provisions

- Income under the head Salaries: Loss under the head “Profits and gains of business or profession” cannot be set off from income under the head “Salaries”

11.3 Carry Forward of Loss

- Loss under the head ‘Income from house property’ [Sec. 71B]
- Loss under head “Profits and gains of business or profession” other than speculation loss [Sec. 72]
- Loss from speculation business [Sec. 73]
- Loss from specified business covered u/s 35AD [Sec. 73A] Loss under the head ‘Capital gains’. [Sec. 74]
- Loss from ‘Activity of owning and maintaining race horses’. [Sec. 74A]

LOSS UNDER THE HEAD	Period for which carry-forward shall be allowed
LOSS UNDER THE HEAD ‘INCOME FROM HOUSE PROPERTY’ [SEC. 71B]	8 assessment years immediately succeeding the assessment year in which such loss is first computed.
CARRY FORWARD & SET OFF OF BUSINESS LOSS OTHER THAN SPECULATION LOSS [SEC. 72]	8 assessment years immediately succeeding the assessment year in which such loss is first computed.
Set off of losses relating to the year of closure of business against deemed profit [Sec. 41(5)]	carried forward for any number of years (without restriction of 8 years) against income chargeable to tax

Loss under the head ‘Income from house property’:

- Can be carried forward and can be set off against income under the same head only.
- Can be carried-forward for 8 assessment years immediately succeeding the assessment year in which such loss is first computed.
- Loss under the head ‘Income from house property’ can be carried forward even when a belated return is filed [as sec. 80 and 139(3) are not applicable to sec. 71B].

Loss under the head “Profits and gains of business or profession” (other than speculation loss)

- can be carried forward and set off against income under the same head.
- business profit includes profits derived from a business activity but assessable under the heads other than ‘Profit and gains of business or profession’, e.g. Dividend income when shares are held as stock, though taxable under the head ‘Income from other sources’ but business loss can be set off against such income.
- Can be carried-forward for 8 assessment years immediately succeeding the assessment year in which such loss is first computed.
- In the assessment year 2022-23, losses prior to the assessment year 2014-2015 cannot be set off.

Exceptions to the above period

1. Closure of business due to specified reasons [Sec. 33B] Situation: Where any loss remains unabsorbed of a business undertaking, which is discontinued due to damages caused by –

- flood, typhoon, hurricane, cyclone, earthquake or other convulsion of nature; or
- riot or civil disturbance; or
- accidental fire or explosion; or

Income Tax Law and Practice

(iv) action by an enemy or action taken in combating an enemy (whether with / without a declaration of war)

- Condition: Such business is re-established, reconstructed or revived by the assessee, within a period of 3 years from the end of the previous year in which such mishap took place.
- Treatment: Losses of such business [including the past eligible losses (to be carried forward)] shall be adjusted with profit of the year in which business is so revived and if the loss cannot be wholly setoff, then it shall further be allowed to be carried forward for 7 years

2. Set off of losses relating to the year of closure of business against deemed profit [Sec. 41(5)]

Situation: Where any part of loss (not being a speculation loss), which arose during the previous year remains unabsorbed in the previous year in which business ceased to exist.

Treatment: Such loss shall be allowed to be carried forward for any number of years (without restriction of 8 years) against income chargeable to tax u/s 41(1); (3); (4); (4A).

Taxpoint: Such loss can be set off even if the return of loss is not submitted in time

1. Business need not be continued: The business losses can be carried forward, even the business in respect of which the loss was originally computed, is not carried on during the previous year.

2. Filing of return in time: As per sec. 80, the business loss cannot be carried forward unless it is determined in pursuance of a return filed by the assessee u/s 139(3), within time as prescribed u/s 139(1).

3. Treatment of unabsorbed depreciation, etc.: Unabsorbed depreciation, unabsorbed scientific research expenditure and unabsorbed family planning expenditure are not covered by sec. 72. Such losses can be carried forward for any number of years.

4. Order of set off: In case of insufficient profit, losses shall be set off in the following order:

(a) Current year's depreciation [Sec. 32(1)], capital expenditure on scientific research [Sec. 35(1)] and capital expenditure on family planning [Sec. 36(1)(ix)];

(b) Brought forward business or profession losses [Sec. 72(1)],

(c) Unabsorbed depreciation [Sec. 32(2)], unabsorbed expenditure on family planning [Sec. 36(1)(ix)], unabsorbed capital expenditure on scientific research [Sec. 35(4)]

- Loss from specified business covered u/s 35AD (i.e. cold chain facility, cross-country natural gas pipeline, etc.) shall be adjusted only from profit from specified business [Further refer sec.73A]. 6. Assessee must be same who incurred the loss: Business losses can be carried forward and set off against the profits of the assessee who incurred the loss i.e. assessee must be same to carry forward the loss. However, this rule has the following exceptions -
- Assessee must be same who incurred the loss:
 - Business losses can be carried forward and set off against the profits of the assessee who incurred the loss i.e. assessee must be same to carry forward the loss.
 - exceptions -
 - Amalgamation
 - Succession
 - Inheritance
 - Demerger

(a) Amalgamation: Business losses and unabsorbed depreciation of an amalgamating company can be setoff against the income of the amalgamated company if the amalgamation is within the meaning of sec. 72A of the Income Tax Act.

(b) Succession: Business losses and unabsorbed depreciation of a proprietary concern or a partnership firm or a specified company succeeded by a company or limited liability partnership as per sec. 47(xiii), (xiii b) and (xiv), can be carried forward by succeeded company or limited liability partnership. (c) Inheritance: As per sec. 78(2), where the assessee acquires the business through inheritance, losses of such business may be carried forward for balance number of years. (d)

Unit 11: Set-off Inter Head Provisions, Set-off Intra Head Provisions

Demerger: In case of demerger, loss of demerged company shall be carried forward and set-off by resulting company.



Note: In following case losses cannot be carried forward

- Business, of an HUF where the business of the HUF is taken over by the Karta of HUF;
- Proprietorship business taken over by a firm in which proprietor is one of the partner;
- A firm being succeeded by another firm;
- A firm where the business of the firm is taken over by one of the partner of the firm,

Set Off and Carry Forward of Unabsorbed Depreciation

- Unabsorbed depreciation shall be allowed to be carried forward for any number of years and such carried forward unabsorbed depreciation may be set off against any income, other than –
- Income under the head “Salaries”
- Winning from lotteries, cross word puzzles, etc.
- Tax point: Unabsorbed depreciation shall be allowed to be carried forward for any number of years and such carried forward unabsorbed depreciation may be set off against any income, other than–
 - Income under the head “Salaries”
 - Winning from lotteries, cross word puzzles, etc
- Notes:
 1. Continuation of business: Unabsorbed depreciation can be carried forward even if the business in respect of which the loss was originally computed, is not carried on during the previous year.
 2. Filing of return: Unabsorbed depreciation can be carried forward even if the return of income has not been filed within time

Carry Forward and Set Off of Speculation Loss [Sec. 73]

Speculative transaction means a transaction in which contract for purchase and sale of any commodity including stock and shares, is periodically or ultimately settled otherwise than by the actual delivery or transfer of the commodity or scripts. [Sec. 43(5)] 2. As per explanation to sec. 73, where any part of the business of a company consists of purchase and sale of shares of other companies, such company shall be deemed to be carrying on speculation business to the extent of purchase and sale of shares. However, this rule is not applicable in case of companies - (a) of which gross total income mainly consists of income which is chargeable under the head “Income from house property”, “Capital gains”, and “Income from other sources”; or (b) of which principal business is the business of trading in shares or banking or granting of loans and advances. Notes: Above explanation covers only transactions of purchase and sale of shares. Debentures, units of UTI or of Mutual Funds are not covered by this explanation

- Losses from speculative transactions or business can be carried forward and set off against income from speculative business only.
- Period for which carry forward shall be allowed: 4 assessment years immediately succeeding the assessment year in which such loss is first computed.
- Academic note: In the assessment year 2022-23, losses prior to the assessment year 2018-19 cannot be set off.
- As per sec. 73(3) in respect of allowance on account of depreciation or capital expenditure on scientific research, the provisions of sec. 73 shall not apply it can be carried forward to any number of years
- It is not necessary that the same speculation business must be continued in the year of carry forward and set off of the losses.

Income Tax Law and Practice

- As per sec. 80, the loss cannot be carried forward unless it is determined in pursuance of a return filed by the assessee u/s 139(3), within time as prescribed u/s 139(1)
- An eligible transaction in respect of trading in derivative referred to in sec.2(ac) of the Securities Contracts (Regulation) Act, 1956 carried out in a recognised stock exchange shall not be treated as speculative transaction.
- Similarly, an eligible transaction in respect of trading in commodity derivatives carried out in a recognised stock exchange (and liable for Commodities Transaction Tax in case of trading in commodity derivatives other than agricultural commodity derivatives) shall not be treated as speculative transaction.
- In respect of trading in agricultural commodity derivatives, the requirement of chargeability of commodity transaction tax is not applicable.
- Loss arising from illegal speculative business cannot be carried forward to the subsequent years for set off against the profits of another speculative business.

Carry Forward & Set Off of Loss from Specified Business Covered U/S 35ad [SEC. 73a]

- Losses from specified business covered u/s 35AD can be carried forward and set off against income from other specified business (whether eligible for deduction u/s 35AD or not)
- No time limit is prescribed for carry forward.
- Filing of return: within time as prescribed u/s 139(1)

Carry Forward and Set Off of Capital Loss [Sec. 74]

- Losses under the head 'Capital gains' can be carried forward and set off against income under the same head,
- loss on transfer of long-term capital assets can be set off only against long term capital gain. T
- Loss on transfer of short-term capital assets can be set off against any income under the head capital gain (whether short-term or long-term).
- Period for which carry-forward shall be allowed: 8 assessment years immediately succeeding the assessment year in which such loss is first computed.
- In the assessment year 2022-23, losses prior to the assessment year 2014-2015 cannot be set off.
- Filing of return: As per sec. 80, the loss cannot be carried forward unless it is determined in pursuance of a return filed by the assessee u/s 139(3), within time as prescribed u/s 139(1).

Carry Forward and Set Off of Losses from Activity of Owning and Maintaining Race Horses [SEC. 74a]

- Period for which carry forward shall be allowed: 4 assessment years immediately succeeding the assessment year in which such loss is first computed.
- Activity of owning and maintaining race horses must be carried on by the assessee in the previous year in which set off is claimed.
- Treatment of other race animals: Sec. 74A states only about losses from activity of owning and maintaining race horses, other race animals are governed by sec. 72.
- To claim benefit of carry forward, return of loss u/s 139(3) must be filed within time as per sec. 139(1).
- Horse race means a race upon which wagering or betting on horses may be lawfully made

Term	Meaning
Amount of loss incurred by the assessee in the activity of owning and maintaining racehorses	(i) In case assessee has no income by way of stake money – amount of revenue expenditure incurred by the assessee wholly & exclusively for the purpose of maintaining race

Unit 11: Set-off Inter Head Provisions, Set-off Intra Head Provisions

	horses.
	(ii) In case assessee has income by way of stake money - The amount by which such income by way of stake money falls short of the amount of revenue expenditure incurred by the assessee wholly & exclusively for the purpose of maintaining race horses. i.e., Loss = Stake money - revenue expenditure for the purpose of maintaining race horses.
Horse race	A horse race upon which wagering or betting maybe lawfully made.
Income by way of stake money	The gross amount of prize money received on a race horse or race horses by the owner thereof on account of the horse or horses or anyone or more of the horses winning or being placed second or in any lower position in horse races.

CARRY FORWARD & SET-OFF OF LOSSES OF FIRM ON CHANGE IN CONSTITUTION OF FIRM [SEC. 78]

- Where a change occurs in the constitution of firm, on account of retirement or death of a partner, the proportionate loss of the retired or deceased partner shall not be carried forward.
- This section shall not apply in case of change in profit sharing ratio or admission of partner.

CARRY FORWARD & SET OFF OF LOSS IN CASE OF CLOSELY HELD COMPANIES [SEC. 79]

- In case of a company in which public are not substantially interested (even the same is eligible start-up company),
- no loss shall be carried forward and set off against the income of the previous year,
- unless at least 51% of the voting power of the company are beneficially held (on the last day of the previous year in which the loss is sought to be set off) by the same person(s) who held at least 51% of the shares on the last day of the financial year in which the loss was incurred.
- Option for eligible start-up company: In the case of eligible start-up company, not being a company in which the public are substantially interested, the loss incurred in any year prior to the previous year shall be carried forward and set off against the income of the previous year, if:
 - All the shareholders of such company who held shares carrying voting power on the last day of the year or years in which the loss was incurred continue to hold those shares on the last day of such previous year; and
 - Such loss has been incurred during the period of 7 years beginning from the year in which such company is incorporated.
- Exceptions
 - Transfer due to death
 - Transfer by way of gift
 - Amalgamation or demerger of foreign company
 - Insolvency and Bankruptcy Code, 2016
 - Relocation of Fund
 - Distressed Company
- Change in the shareholding due to following reasons shall not be considered¹.
- Transfer due to death: Where a change in the said voting power takes place in a previous year consequent upon the death of a shareholder

- Transfer by way of gift: Where a change in the said voting power takes place in a previous year on account of transfer of shares by way of gift to any relative of the shareholder making such gift
- Amalgamation or demerger of foreign company: Any change in the shareholding of an Indian company which is a subsidiary of a foreign company as a result of amalgamation or demerger of a foreign company subject to the condition that 51% shareholders of the amalgamating or demerged foreign company continues to be the shareholder of the amalgamated or the resulting foreign company.
- Insolvency and Bankruptcy Code, 2016: Where a change in the shareholding takes place in a previous year pursuant to a resolution plan approved under the Insolvency and Bankruptcy Code, 2016, after affording a reasonable opportunity of being heard to the jurisdictional Principal Commissioner or Commissioner
- Relocation of Fund: The section is not applicable to a case to the extent that a change in the shareholding has taken place during the previous year on account of relocation referred to in the Explanation to sec. 47(viiac) and (viid).
- Distressed Company: The provision is not applicable to a company, and its subsidiary and the subsidiary of such subsidiary, where: The National Company Law Tribunal (NCLT), on an application moved by the Central Government u/s 241 of the Companies Act, 2013, has suspended the Board of Directors of such company and has appointed new directors nominated by the Central Government, u/s 242 of the said Act; and (ii) a change in shareholding of such company, and its subsidiary and the subsidiary of such subsidiary, has taken place in a previous year pursuant to a resolution plan approved by the Tribunal u/s 242 of the Companies Act, 2013 after affording a reasonable opportunity of being heard to the jurisdictional Principal Commissioner or Commissioner.
- Notes: (a) Losses under the head 'Capital gains': Sec. 79 applies to all losses, including losses under the head Capital gains. (b) Unabsorbed depreciation: The above provision is not applicable on unabsorbed depreciation; such unabsorbed depreciation shall be allowed to be carried forward.

Carry Forward & Set Off of Accumulated Loss and Unabsorbed Depreciation in Case of Amalgamation

- Applicability: Sec. 72A is applicable on following amalgamation, where -
 1. There has been an amalgamation of a company owning - • an industrial undertaking; or • a ship; or • a hotel, with another company; or
 2. There has been amalgamation of a banking company with a specified bank.
 3. There has been amalgamation of one or more public sector company or companies with one or more public sector company or companies; or
 4. There has been amalgamation of an erstwhile public sector company with one or more company or companies, if the share purchase agreement entered into under strategic disinvestment restricted immediate amalgamation of the said public sector company and the amalgamation is carried out within 5 years from the end of the previous year in which the restriction on amalgamation in the share purchase agreement end
- The amalgamated company owns the industrial undertaking of the amalgamating company;
- The amalgamated company achieves the level of production of at least 50% of the installed capacity of the said undertaking before the end of the 4 years from the date of amalgamation and continue to maintain the said minimum level of production till the end of 5 years from the date of amalgamation;

Unit 11: Set-off Inter Head Provisions, Set-off Intra Head Provisions

Account must be verified by an accountant & a certificate in Form 62 shall be furnished along with the return of income for the assessment year relevant to the previous year during which the prescribed level of production is achieved & for subsequent assessment years relevant to the previous year falling within 5 years from the date of amalgamation

Conditions for Carry forward & set off of accumulated loss and unabsorbed depreciation allowable in case of amalgamation

- The amalgamating company - • has been engaged in the business (in which the accumulated loss occurred or depreciation remains unabsorbed) for three or more years; • has held continuously as on the date of the amalgamation at least 3/4th of the book value of fixed assets held by it 2 years prior to the date of amalgamation.
- The amalgamated company – • holds continuously for a minimum period of 5 years from the date of amalgamation at least 3/4th of the book value of fixed assets of the amalgamating company acquired in a scheme of amalgamation; • continues the business of the amalgamating company for a minimum period of 5 years from the date of amalgamation; • fulfils such other conditions# as may be prescribed to ensure the revival of the business of the amalgamating company or to ensure that the amalgamation is for genuine business purpose.”
- The accumulated loss and the unabsorbed depreciation of the amalgamating company shall be deemed to be the loss or depreciation of the amalgamated company for the previous year in which the amalgamation was effected.
- Consequences if the conditions are not satisfied
- As per sec. 72A (3), in a case where above conditions are not complied with, the set off of loss or depreciation made in any previous year by the amalgamated company shall be deemed to be the income of the amalgamated company and chargeable to tax in the year in which such conditions are violated

Carry Forward & Set Off of Accumulated Loss and Unabsorbed Depreciation in Case of Demerger [Sec. 72a (4)]

- Where such loss or unabsorbed depreciation is directly related to the undertakings transferred to the resulting company:
 - Such loss shall be allowed to be carried forward and set off in the hands of the resulting company

Where such loss or unabsorbed depreciation is not directly related to the undertakings transferred to the resulting company:

- Such loss shall be
- apportioned between the demerged company and the resulting company in the same proportion in which the assets of the undertakings have been retained by the demerged company and transferred to the resulting company; and
- allowed to be carried forward and set off in the hands of the demerged company or the resulting company.

CARRY FORWARD & SET OFF OF LOSSES ON CONVERSION OF PROPRIETARY CONCERN OR PARTNERSHIP FIRM INTO COMPANY [SEC. 72A (6)]

- a firm is succeeded by a company fulfilling the conditions laid down in sec. 47(xiii); or
- a proprietary concern is succeeded by a company fulfilling conditions laid down in sec. 47(xiv).
- The accumulated loss and unabsorbed depreciation of the predecessor firm or the proprietary concern, as the case may be, shall be deemed to be the loss or allowance for depreciation of the successor company for the purpose of previous year in which reorganisation of business was effected.

Income Tax Law and Practice

- Accumulated loss of such firm or concern can be carried forward for further 8 years

Order of Set-Off of Losses

- Current year depreciation [Section 32(1)];
- Current year capital expenditure on scientific research and current year expenditure on family planning, to the extent allowed.
- Brought forward loss from business/profession [Section 72(1)];
- Unabsorbed depreciation [Section 32(2)];
- Unabsorbed capital expenditure on scientific research [Section 35(4)];
- Unabsorbed expenditure on family planning [Section 36(1)(ix)].

Submission of Return of Losses [Section 80]

- As per section 80,
 - business loss under section 72(1),
 - speculation business loss under section 73(2),
 - loss from specified business under section 73A(2),
 - loss under the head "Capital Gains" under section 74(1) and
 - loss from activity of owning and maintaining race horses under section 74A (3),
- which has not been determined in pursuance of a return filed under section 139(3) can not be carried forward and set-off. Thus, the assessee must have filed a return of loss under section 139(3) in order to carry forward and set off of such losses.
- Such a return of loss should be filed within the time allowed under section 139(1).
- However, this condition does not apply to a loss from house property carried forward under section 71B and unabsorbed depreciation carried forward under section 32(2).

Illustration 1

Particulars	
Income from salary (computed)	1,35,000
Loss from house property	72,000
Loss from non-speculative business	66,000
Loss from speculative business	12,000
Short-term capital losses	75,000
Long-term capital gains taxable u/s 112	57,000

Solution

Particulars	Amount (₹)	Amount (₹)
Income from salaries	1,35,000	
set off of loss from house property	-72,000	63,000
Profits and gains of business and profession		
Speculative loss to be carried forward	22,000	
Business loss to be carried forward	4,000	

Unit 11: Set-off Inter Head Provisions, Set-off Intra Head Provisions

Capital Gain		
Long term capital gain taxable u/s 112	57000	
Short term capital loss 75,000 set off against long-term capital gains to the extent of 57,000	-57000	
Balance short term capital loss of 18000 to be carried forward		
Taxable income		63000

- Business loss cannot be set-off against salary income.
- Loss from the speculative business can be set off only against the income from the speculative business. Hence, such loss has to be carried forward.
- Short term capital loss can be set off against both short term capital gain and long-term capital gain.

Illustration 2

Particulars	
Income from salary (computed)	6,00,000
Loss from let-out property	3,20,000
Business loss	1,20,000
Bank interest (FD) received	90,000

Solution

Particulars	Amount ()	Amount ()
Income from salary	6,00,000	
Less: Loss from house property of 3,20,000	(-) 2,00,000	4,00,000
HP loss of 1,20,000 to be carried forward to next assessment year		
Income from other sources (interest on fixed deposit with bank)	90,000	
Business loss of 1,20,000 set-off to the extent of	(-) 90,000	-
Business loss of 30,000 to be carried forward for set-off against business income of the next assessment year		
Gross total income		4,00,000
Less: Deduction under Chapter VI-A		Nil

Income Tax Law and Practice

Total income		2,00,000
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Illustration 3

Particulars		`
STCG		3,00,000
LTCL of A.Y.2020-21		-1,92,000
STCL of A.Y.2021-22		-74,000
LTCG u/s 112		1,50,000

Solution

Particulars	`	`
STCG	3,00,000	
Less: STCL of A.Y.2021-22	-74000	
STCG		2,26,000
LTCG u/s 112	1,50,000	
LTCL of A.Y.2020-21	1,50,000	
LTCG		Nil
Taxable short-term capital gains		2,26,000

Illustration 4

Particulars		`
Income from the activity of owning and maintaining the race horses		2,25,000
Income from cotton business		2,55,000
Brought forward cotton business loss (A.Y. 2021-22)		1,50,000
Brought forward(from A.Y.2019-20) loss from the activity of owning and maintaining the race horses		2,88,000

Solution

Particulars	`	`
Income from the activity of owning and maintaining race horses	2,25,000	
Less: Brought forward loss of 2,88,000 from the activity of owning and maintaining race horses	2,25,000	Nil
Balance loss of 63,000 from the activity of owning and maintaining race horses to be carried forward to A.Y.2023-24		

Unit 11: Set-off Inter Head Provisions, Set-off Intra Head Provisions

Income from cotton business	2,55,000	
Brought forward cotton business loss (A.Y. 2021-22)	150000	
Total income		1,05,000

Illustration 5

Particulars	
Income from salaries (computed)	450000
Income from speculation business	180000
Loss from non-speculation business	120000
Short term capital gain	240000
Long term capital loss of A.Y.2020-21	90000
Winning from lotteries (Gross)	60000

Solution

Particulars		
Income from salaries		450000
Income from speculation business	180000	
Less : Loss from non-speculation business	120000	60,000
Short-term capital gain		240000
Winnings from lotteries		60000
Taxable income		8,10,000

Summary

Profit and losses are two sides of a coin. Losses, of course, are hard to digest. However, the Income-tax law in India does provide taxpayers some benefits of incurring losses too. The law contains provisions for set-off and carry forward of losses which are discussed in detail in this unit. Set off of losses means adjusting the losses against the profit or income of that particular year. Losses that are not set off against income in the same year can be carried forward to the subsequent years for set off against income of those years. A set-off could be an intra-head set-off or an inter-head set-off. After making the appropriate and permissible intra-head and inter-head adjustments, there could still be unadjusted losses. These unadjusted losses can be carried forward to future years for adjustments against income of these years. The rules as regards carry forward differ slightly for different heads of income.

Keywords

Intra-head Set off: The losses from one source of income can be set off against income from another source under the same head of income.

Inter-head Set off: After the intra-head adjustments, the taxpayers can set off remaining losses against income from other heads.

Income Tax Law and Practice

Speculative Income: A speculative transaction is a transaction of purchase or sale of a commodity including stocks and shares settled **otherwise than by actual delivery or transfer of the commodity or scrip** (Section 43(5) of the Income-tax Act)

Self Assessment

1. The process of adjustment of loss from a source under a particular head of income against income from other source under the same head of income is called _____. (a) Inter-head adjustment (b) Intra-head adjustment (c) Carry forward of loss (d) Clubbing of income
 - A. Inter-head adjustment
 - B. Intra-head adjustment
 - C. Carry forward of loss
 - D. Clubbing of income

2. While making intra-head adjustment, loss from the business of owning and maintaining race horses can be set off against...only.
 - A. Income from winnings from lotteries
 - B. Income from crossword puzzles _____ only.
 - C. Income from business of owning and maintaining race horses
 - D. Income from card game

3. However, if loss under the head "Income from house property" cannot be fully adjusted in the year in which such loss is incurred, then unadjusted loss can be carried forward for incurred. _____ years immediately succeeding the year in which the loss is
 - A. 2
 - B. 5
 - C. 8
 - D. 10

4. In case of a Company, being a company in which public are not substantially interested but not being an eligible start-up as referred to in section 80-IAC, if the person beneficially holding _____ of the voting power as on the last day (i.e. 31st March) of the year in which the loss was incurred and on the last day (i.e. 31st March) of the year in which the company wants to set off the brought forward loss are different, then the company cannot set off such brought forward loss.
 - A. 20%
 - B. 25%
 - C. 50%
 - D. 51%

5. Unabsorbed depreciation can be carried forward for:
 - A. No time limit
 - B. 4 years
 - C. 6 years
 - D. 8 years

6. Loss from specified business can be carried forward for:
 - A. No time limit

Unit 11: Set-off Inter Head Provisions, Set-off Intra Head Provisions

- B. 4 years
 - C. 6 years
 - D. 8 years
7. STCL can be carried forward for:
- A. No time limit
 - B. 4 years
 - C. 6 years
 - D. 8 years
8. LTCL can be carried forward for:
- A. No time limit
 - B. 4 years
 - C. 6 years
 - D. 8 years
9. Loss from normal business can be carried forward for:
- A. No time limit
 - B. 4 years
 - C. 6 years
 - D. 8 years
10. Loss from house property can be carried forward for:
- A. No time limit
 - B. 4 years
 - C. 6 years
 - D. 8 years
11. Which of the following is not true about loss from owning and maintaining race-horses?
- A. Can be carry forward up to next 4 assessment years from the assessment year in which the loss was incurred.
 - B. Cannot be carried forward if the return is not filed within the original due date.
 - C. Can only be set off against income from owning and maintaining race-horses only.
 - D. Can be carried forward if the return is not filed within the original due date
12. Which of the following is not true about capital losses?
- A. Can be carry forward up to next 4 assessment years from the assessment year in which the loss was incurred
 - B. Long-term capital losses can be adjusted only against long-term capital gains
 - C. Short-term capital losses can be set off against long-term capital gains as well as short-term capital gains
 - D. Cannot be carried forward if the return is not filed within the original due date.
13. Which of the following is not true about speculative business loss?
- A. Can be carry forward up to next 4 assessment years from the assessment year in which the loss was incurred
 - B. Can be adjusted only against Income from speculative business

Income Tax Law and Practice

- C. Can be carried forward if the return is not filed within the original due date
 D. Not necessary to continue the business at the time of set off in future year.
14. Which of the following is not true about non-speculative business loss?
 A. Can be carry forward up to next 4 assessment years from the assessment year in which the loss was incurred
 B. Can be adjusted only against Income from business or profession.
 C. Can be carried forward if the return is not filed within the original due date
 D. Not necessary to continue the business at the time of set off in future year.
15. Which of the following is not true about house property loss?
 A. Can be carry forward up to next 8 assessment years from the assessment year in which the loss was incurred
 B. Can be adjusted only against income form house property.
 C. Can be carried forward even if the return of income for the loss year is belatedly filed
 D. Can be adjusted against any income.

Answers for Self Assessment

- | | | | | |
|-------|-------|-------|-------|-------|
| 1. B | 2. C | 3. C | 4. D | 5. A |
| 6. A | 7. D | 8. D | 9. D | 10. D |
| 11. D | 12. A | 13. C | 14. A | 15. D |

Review Questions

1. What do you mean by "Set-off and carry forward of losses"?
2. Which losses can be carried forward?
3. Write a note on Carry-forward and set-off of losses in case of succession of business or profession.
4. Write a note on Carry forward and set off of accumulated losses and unabsorbed depreciation in case of demerger.
5. Write a note on Carry forward and set off of accumulated loss and unabsorbed depreciation in case of amalgamation.

**Further Readings**

- https://www.icsi.edu/media/webmodules/16112021_Advance_Tax_Laws.pdf
- Income Tax Law & Practice A.Y 2021-22 by Dr H.C. Mehrotra and Dr. S. P. Goyal. Sahitya Bhawan Publications
- Study Material on Direct Tax Laws and International Taxation by ICAI
- Direct Tax Laws and Practice by Dr. Girish Ahuja & Dr. Ravi Gupta
- <https://incometaxindia.gov.in/Tutorials/21-%20MCQ%20set%20off%20and%20carry%20frwrdrd.pdf>

Unit 12: Deductions from Total Income Law

CONTENTS

Objectives

Introduction

12.1 Deductions Not Available From:

12.2 Deduction U/S 80C in Respect of LIC Premium, Contributions To PF, ETC

12.3 Deduction U/S 80CC In Respect of Contribution To Pension Fund

12.4 Deduction U/S 80CC In Respect of Contribution To Pension Fund

12.5 Deduction U/S 80CCE: Limit on Deductions U/S 80C, 80CCC and 80CCD

12.6 Deduction U/S 80D In Respect of Medical Insurance Premium

12.7 Deduction U/S 80E In Respect Repayment of Loan For Higher Education

12.8 Deduction in Respect of Interest on Deposits in Savings Account [SEC. 80TTA]

12.9 Deduction in Respect of Income of Producer Companies [SEC. 80PA]

12.10 Deduction in Respect of Inter-corporate Dividend [SEC. 80M]

12.11 Deduction U/S 80JJA in Respect of Profits and Gains of Business of Collecting and Processing of Bio-degradable Waste

12.12 Deduction in Respect of Profits and Gains from Housing Projects [SEC. 80-IBA] Amended

12.13 Special Provisions In Respect Of Certain Undertakings In North- Eastern States [SEC. 80-IE]

12.14 Deduction U/S 80JJAA in Respect of Employment of New Workmen

12.15 Deduction U/S 80QQB in Respect of Royalty Income of Authors of Books

12.16 Deduction U/S 80RRB in Respect of Royalty on Patents

12.17 Deduction in Respect of Interest on Deposits in Case of Senior Citizens [SEC. 80TTB]

12.18 Rebates and Reliefs.

Summary

Keywords

Self Assessment

Answers for Self Assessment

Review Questions

Further Readings

Objectives

After studying this unit, you will be able to:

- understand the Deductions in computing total income
- understand the concept of Rebates and Reliefs.

Introduction

Deductions assist in lowering a person's taxable income. It aids in tax burden reduction overall and tax savings for an individual. Only when the GI is positive are deductions possible. A deduction is allowed under Section 80C for investments made in certain assets up to a limit of one lakh fifty

Income Tax Law and Practice

thousand rupees by both individuals and Hindu undivided families. In no case can the total deductions allowed under Sections 80C, 80CCC, and 80CCD (1) exceed Rs. 1,50,000. If a resident individual's total income is less than 5,000,000, they are eligible for an income tax rebate under Section 87A. The rebate is equal to the lesser of Rs. 12,500 or 100% of the income tax. Prior to determining the health and education cess, it is deducted from income tax. [Amendment by Finance (No.2) Act, 2019]. Anyone who received any portion of their income in advance or arrears or who received profit in place of wages the previous year is given relief under Section 89. The Assessee may submit an application to the Assessing Officer, who is authorized by Rule 21AA of the Income-tax Rules, 1962, to give relief in appropriate circumstances. Any amount received or due by an assessee upon voluntary retirement or termination of employment under any scheme or schemes for voluntary retirement, or, in the case of a public sector company mentioned in sub clause I of clause (10C) of section 10, under a scheme for voluntary separation, shall not be subject to such relief if the assessee has requested an exemption under paragraph (10C) of section 10 for such or any other assessment year with respect to any sum received or receivable upon such voluntary retirement, termination of his service, or voluntary separation. Basic Rules

12.1 Deductions Not Available from:

- long-term capital gain;
- short term capital gain covered u/s 111A (i.e., STCG on which STT is charged); and
- casual income like winning from lotteries, races, etc.

Limit of deduction: The aggregate amount of deduction under chapter VIA cannot exceed the Gross Total Income of the assessee excluding –

- Long- term capital gain;
- Short-term capital gain covered u/s 111A;
- casual income like winning from lotteries, card games, horse races, etc.; and
- income referred in Sec.115A, 115AB, 115AC, 115ACA.
- Deduction under chapter VIA shall be available only if the assessee claims for it.
- Where a deduction under any section of chapter VIA has been claimed then the same shall not qualify for the deduction in any other section.

12.2 Deduction U/S 80C in Respect of LIC Premium, Contributions To PF, ETC

Applicable to:

- An Individual or a Hindu Undivided Family (whether resident or non-resident)

Applicable to Individual & HUF both:

- Life insurance premium paid by a person to effect or to keep in force an insurance policy (life policy or endowment policy) [Sec. 80C(2)(i)]:

Insurance policy can be taken on a life of the following:

- a. In case of an individual: Himself, spouse, and child (whether major or minor) of such individual;
- b. In case of HUF: Any member of the HUF.

Maximum limit:

Premium on insurance policy in excess of following % of the actual sum assured shall be ignored.

Policy issued:

Up to 31-03-2012: 20%

During P.Y. 2012-13: 10%

On or after 01-04-2013

Unit 12: Deductions from total income Law

Insured is disable or suffering from disease specified u/s 80DDB: 15%

Insured is any other person: 10%

Contribution made towards Public provident fund (PPF). [Sec. 80C (2) (v)]:

1. Subscription should be in the name of the following persons:
 - a. In case of an individual: Such individual, his spouse, and child (whether major or minor);
 - b. In case of HUF: Any member of HUF.
2. Contribution must not be in form of repayment of the loan

Any subscription to National Savings Certificates, VIII Issue and IX Issue [Sec. 80C(2)(ix)]

Contribution for participating in the Unit-linked Insurance Plan (ULIP) of Unit Trust of India (UTI) or ULIP of LIC Mutual fund u/s 10(23D) formerly known as Dhanraksha 1989. [Sec.80C(2)(x)]

Sum paid to effect or keep in force a contract for notified annuity plan of the LIC or any other insurer. [Sec. 80C(2)(xii)]

Subscription to notified units of a specified Mutual fund u/s 10(23D)/ administrator or the specified company as referred in sec. 2 of UTI. [Sec. 80C(2)(xiii)]

Any sum paid as a subscription to the Home Loan Account Scheme or notified pension fund of the National Housing Bank. [Sec 80C(2) (xv)]

Any sum paid as a subscription to a notified deposit scheme. [Sec. 80C(2)(xvi)]

Any payment for purchase or construction of residential house property (the income from which is chargeable to tax under the head "Income from house property), by way of -

- An any instalment due under any self-financing or another scheme of any development authority, housing board, or other authority engaged in the construction and sale of house property on an ownership basis; or
- any instalment due to any company or co-operative society of which the assessee is a shareholder or member towards the cost of the house property allotted to him; or
- repayment of the amount borrowed by the assessee from specified person#
- stamp duty, registration fee, and other expenses for the purpose of transfer of such house property to the assessee [Sec. 80C(2)(xviii)]

Any amount invested in -

- Debentures of or equity shares in an eligible issue of capital; or
- Eligible issue of capital of any public financial institution. [Sec. 80C(2)(xix)]
- Subscription to units of any mutual fund u/s 10(23D) provided an amount of subscription to such units is subscribed only in the eligible issue of capital [Sec. 80C(2)(xx)]
- Investment as a term deposit for a period of 5 years or more with a scheduled bank. [Sec. 80C(2) (xxi)]
- Notified Bonds issued by the National Bank for Agriculture and Rural Development (NABARD) [Sec. 80C(2)(xxii)]
- Senior Citizens Savings Scheme Rules, 2004 [Sec. 80C(2)(xxiii)]
- 5 -year time deposit in an account under the Post Office Time Deposit Rules, 1981 [Sec. 80C(2)(xxiv)]

Quantum of deduction:

- Deduction under this section shall be a minimum of the following:
- Aggregate of the eligible contributions, expenditures, or investments (discussed above) • 1,50,000

12.3 Deduction U/S 80CC In Respect of Contribution To Pension Fund

Applicable to an individual (irrespective of residential status or citizenship of the individual)

Condition to be satisfied:

1. Amount paid under an annuity plan: During the previous year, the assessee has paid or deposited a sum under an annuity plan of the Life Insurance Corporation of India (LIC) or any other insurer for receiving a pension from the fund referred to in Sec. 10(23AAB).
2. Payment out of taxable income: The amount must be paid out of income that is chargeable to tax. However, it is not necessary that such income relates to the current year.

Quantum of deduction Minimum of the following -

- a) Amount deposited; or
- b) 1,50,000

12.4 Deduction U/S 80CC In Respect of Contribution To Pension Fund

Applicable to an individual

Condition to be satisfied

During the previous years, the assessee has paid or deposited any amount in his account under a pension scheme notified by the Central Government (New Pension System and Atal Pension Yojna)

Deduction u/s 80CCD (1)

A. In case of salaried individual

Lower of the following

- Amount so paid or deposited
- 10% of his salary¹ in the previous year

Add: Whole of the contribution made by the employer to such account to the maximum of 10% (14% where such contribution is made by the Central Govt.) of his salary¹ in the previous year.

Amount of Deduction

B. In case of other individual

Lower of the following

- Amount so paid or deposited
- 20% of his gross total income in the previous year

Additional Deduction u/s 80CCD(1B) Lower of the following shall also be eligible for deduction • Contribution to the scheme by any individual [Other than the amount claimed and allowed as deduction u/s 80CCD (1)]

50,000

12.5 Deduction U/S 80CCE: Limit on Deductions U/S 80C, 80CCC and 80CCD

Shall not exceed 1,50,000.

12.6 Deduction U/S 80D In Respect of Medical Insurance Premium

Applicable to an individual or an HUF (irrespective of residential status or citizenship)

In case of an Individual:

- Nature of Payment
 - a. Payment of Mediclaim insurance premium#; or

Unit 12: Deductions from total income Law

- b. Contribution to the Central Government Health Scheme or any other notified Health Scheme
- c. Preventive health check-up expenditure
- Expenditure on behalf of: Himself/herself, spouse or dependent children
- Quantum of Deduction;
- Lower of the following:
 - a. Aggregate of – Premium paid; or – Contribution made; or – Preventive health check- up (up to 5,000)
 - b. 25,000 p.a. Senior Citizen Where the person, for whom such premium (not for payment made for preventive health check-up) is paid, is a senior citizen, then the maximum limit of deduction shall be increased to 50,000 instead of 25,000.

In case of an Individual:

- Nature of Payment
 - a. Payment of Mediclaim insurance premium
 - b. Preventive health check-up expenditure
- Expenditure on behalf of: Parents (whether dependent or not)

Quantum of Deduction;

Lower of the following:

- i. Aggregate of – Premium paid; or – Preventive health check up (up to 5,000)
- ii. 25,000 p.a.

12.7 Deduction U/S 80E In Respect Repayment of Loan For Higher Education

Applicable to an Individual (irrespective of residential status and citizenship of the individual).

Conditions to be satisfied

1. Loan from specified institution:

The assessee had taken a loan from –

- A financial institution; or Financial Institution means a banking company to which the Banking Regulation Act, 1949 applies (including any banking institution referred to in sec. 51 of that Act) or any other specified financial institution.
- an approved charitable institution Approved Charitable Institution means an institution established for charitable purposes and approved by the prescribed authority u/s 10(23C) or an institution referred to in Sec. 80G(2)(a)
 1. Purpose of loan: The loan must have been taken for the purpose of pursuing higher education for himself/ herself or for any other following persons:
 - a. Spouse
 - b. Children (dependent or not); or
 - c. the student for whom the individual is the legal guardian
 2. Payment out of taxable income
 3. Quantum of deduction: Amount paid during the year by way of payment of interest.
 4. Maximum permissible period for which deduction is available [Sec.80E(2)]: the initial assessment year and 7 assessment years immediately succeeding the initial assessment year\$ or until interest is paid by the assessee in full, whichever is earlier.

12.8 Deduction in Respect of Interest on Deposits in Savings Account [SEC. 80TTA]

Applicable to: An individual (other than senior citizen covered u/s 80TTB) or a Hindu Undivided Family

Conditions to be satisfied: Gross total income of an assessee includes any income by way of interest on deposits (not being time deposits) in savings account with: –

- a banking company;
- a co-operative society engaged in carrying on the business of banking (including a co-operative land mortgage bank or a co-operative land development bank); or
- a Post Office
- Quantum of deduction: Minimum of the following
 - a. Interest on such deposits in saving account
 - b. 10,000

12.9 Deduction in Respect of Income of Producer Companies [SEC. 80PA]

Applicable to Producer Company as defined u/s 581A of the Companies Act, 2013.

Conditions to be satisfied

- a. Turnover: Total turnover of the assessee is less than 100crores in any previous year.
- b. Profit from eligible business: Gross total income of the assessee includes any income from an eligible business.
- c. the processing of the agricultural produce of the members;

12.10 Deduction in Respect of Inter-corporate Dividend [SEC. 80M]

Applicable to Domestic Company

Conditions to be satisfied

- a. Dividend Income: Gross total income of the assessee includes any income by way of dividends from any other domestic company or a foreign company or a business trust.
- b. Dividend Distribution: The assessee distributes dividends among its shareholder within the due date

Due date means the date one month prior to the due date for furnishing the return of income.

Quantum of Deduction Minimum of the following:

- a. Dividend so received by the assessee; or
- b. Dividend distributed by the assessee within the due date

12.11 Deduction U/S 80JJA in Respect of Profits and Gains of Business of Collecting and Processing of Bio-degradable Waste

Applicable to All assessee

Conditions to be satisfied

- Assessee engaged in the business of collecting and processing or treating bio-degradable waste for –
 - a) generating power; or

Unit 12: Deductions from total income Law

- b) producing bio-fertilizers, bio-pesticides, or other biological agents; or
 - c) producing biogas; or
 - d) making pellets or briquettes for fuel; or
 - e) organic manure.
- Quantum of deduction of 100% of the profit derived from such business for a period of 5 consecutive years from the year of commencement of such business.

12.12 Deduction in Respect of Profits and Gains from Housing Projects [SEC. 80-IBA] Amended

Applicable to All assessee Conditions to be satisfied

1. Housing Project or Rental Housing Project:

- The assessee is engaged in the business of
 - a. developing and building housing projects; or
 - b. developing and building a rental housing project

Housing project shall be a project which fulfills the following conditions:

- a) The project is approved by the competent authority after 01-06-2016, but on or before 31-03-2022.
- b) The project is completed within a period of 5 years from the date of approval by the competent authority.
- c) The carpet area of the shops and other commercial establishments included in the housing project does not exceed 3% of the aggregate carpet area
- d) The project should satisfy certain measurement criteria.
- f) The project is the only housing project on a such plot of land;
- g) The stamp duty value of a residential unit in the housing project does not exceed 45lakhs.
- h) Where a residential unit in the housing project is allotted to an individual, no other residential unit in the housing project shall be allotted to the individual or the spouse or the minor children of such individual;
- i) The assessee maintains separate books of account in respect of the housing project.

Quantum of Deduction 100% of the profits derived from such business.

12.13 Special Provisions In Respect Of Certain Undertakings In North-Eastern States [SEC. 80-IE]

Applicable to All assessee

- Conditions to be satisfied: Time and Nature of business:
- The assessee begins the following activity on 01-04-2007 and 31-03-2017:
 - manufacture or production of any eligible article or thing, or Eligible article or thing means the article or thing other than the following:
 - Tobacco and manufactured tobacco substitutes;
 - Pan masala;
 - Plastic carry bags of less than 20 microns as specified by the Ministry of Environment and Forests; and
 - Goods produced by petroleum oil or gas refineries.
 - undertakes substantial expansion; or Substantial expansion means an increase in the investment in the plant and machinery by at least 25% of the book value of

plant and machinery (before taking depreciation in any year), as on the first day of the previous year in which the substantial expansion is undertaken.

- carry on any eligible business.
 - i. Hotel (not below two-star category);
 - ii. Adventure and leisure sports including ropeways;
 - iii. Providing medical and health services in the nature of a nursing home with a minimum capacity of 25 beds;
 - iv. running an old-age home;
 - v. operating vocational training institute for hotel management, catering, and food craft, entrepreneurship development, nursing and para-medical, civil aviation-related training, fashion designing, and industrial training;
 - vi. running information technology -related training centre;
 - vii. manufacturing of information technology hardware; and
 - viii. Bio-technology

12.14 Deduction U/S 80JJAA in Respect of Employment of New Workmen

Applicable to Any assessee subject to tax audit under sec. 44AB

Conditions to be satisfied for New Business:

- a. Business is not formed by splitting up, or the reconstruction, of an existing business.
 - b. No business reorganization
 - c. Audit:
 - d. Claimed in the return
- Quantum of deduction of 30% of additional employee cost incurred in the course of such business in the previous year, for 3 assessment years including the assessment year relevant to the previous year in which such employment is provided
 - Additional employee does not include:
 - an employee whose total emoluments are more than 25,000 per month; or
 - an employee for whom the entire contribution is paid by the Government under the Employees' Pension Scheme notified in accordance with the provisions of the Employees' Provident Funds and Miscellaneous Provisions Act, 1952; or
 - an employee employed for a period of fewer than 240 days (150 days in case of an assessee who is engaged in the business of manufacturing apparel or footwear or leather products) during the previous year;
 - an employee who does not participate in the recognized provident fund

12.15 Deduction U/S 80QQB in Respect of Royalty Income of Authors of Books

Applicable to: A resident individual (irrespective of his citizenship)

Conditions to be satisfied

1. Profession of assessee
2. Nature of book
3. Nature of income

Quantum of deduction: Deduction in case of lump sum royalty in lieu of all rights of the assessee in the book Minimum of the following –

- a. 100% of such income; or
- b. 3,00,000

12.16 Deduction U/S 80RRB in Respect of Royalty on Patents

Applicable to: A resident individual (irrespective of the citizenship of the individual), being a patentee (i.e. owner or co-owner of a patent)

Conditions to be satisfied

1. Nature of income: Assessee has earned income (either in India or outside India) by way of royalty in respect of a patent registered on or after 1-4-2003 under the Patents Act, 1970.
2. Certificate to be attached: Assessee must furnish a certificate in Form 10CCE duly signed by the prescribed authority along with the return of income.

Quantum of deduction

- Income earned in India:
 - Minimum of the following
 - 100% of such income; or
 - 3,00,000
- Income earned outside India:
 - Minimum of the following
 - Income in respect of money brought into India in convertible foreign exchange within the prescribed time limit; or
 - 3,00,000

12.17 Deduction in Respect of Interest on Deposits in Case of Senior Citizens [SEC. 80TTB]

Applicable to Senior Citizen

Conditions to be satisfied: Gross total income includes any income by way of interest on deposits with: –

- a. A banking company applies;
- b. A co-operative society engaged in carrying on the business of banking (including a co-operative land mortgage bank or a co-operative land development bank); or
- c. A Post Office

Quantum of deduction: Minimum of the following

- a. Interest on such deposits
- b. 50,000

12.18 Rebates and Reliefs.

What is Relief under Section 89 of the Income-tax Act, 1961?

- If an individual receives any portion of his salary in arrears or in advances or receives profit in lieu of salary, he can claim relief in terms of Section 89 with Rule 21A of the Income-tax Rules, 1962.

Computation of relief is being provided in Rule 21A.

Rule 21A (1) reads as follows:

Income Tax Law and Practice

- Where, by reason of any portion of an assessed salary being paid in arrears or in advance or,
- by reason of any portion of family pension received by an assessed being paid in arrears or,
- by reason of his having received in any one financial year salary for more than twelve months or
- a payment which under the provisions of clause (3) of Section 17 is a profit in lieu of salary,
- his income is assessed at a rate higher than that at which it would otherwise have been assessed, the relief be granted under sub-section (1) of Section 89.

When is Relief u/s 89 available?

Relief under section 89 is available when

- Salary is received in arrears or in advance;
- Salary is received for more than 12 months in one financial year;
- Family Pension being received in arrears;
- Gratuity
- Compensation on termination of employment; and
- Commuted Pension
- One important thing to note is that relief can only be claimed if tax payable is actually higher due to receipt of such arrears.
- If there is no extra tax liability, relief is not allowed.

What is “Less: Rebate u/s 87A” reflect in salary slip as per India income tax?

- [Rebate under section 87A](#) means tax rebate available to the resident individuals whose total income does not exceed Rs.5 lakhs.
- For this rebate no additional investment is required.

Things to remember to avail rebate under Section 87A

- Super senior citizens above 80 years of age are not eligible to claim rebates under Section 87A
- The amount of rebate will be lower than the limit specified under Section 87A or total income tax payable (before cess)
- Section 87A rebate is available under old as well as the new tax regime

Rebate against various tax liabilities

- Section 87A rebate can be claimed against tax liabilities on:
 - Normal income which is taxed at the slab rate
 - [Long-term capital gains](#) under Section 112 of the Income Tax Act.
 - [Short-term capital gains](#) under Section 111A of the Act, on which tax is payable at a flat rate of 15%.

Eligibility to claim rebate u/s 87A

- Resident individual
 - Total income after reducing the deductions under Chapter VI-A (Section 80C, 80D and so on) does not exceed Rs 5 lakh in a FY

Summary

Individuals can claim tax deduction benefits for payments made towards life insurance policies, fixed deposits, superannuation/provident funds, tuition fees, and construction/purchase of residential properties under Section 80C of the Income Tax Act. Taxes are an integral component in our country, with them accounting for a major portion of the income earned by the government, income which is utilized to provide certain basic provisions to citizens. Individuals who earn more than a certain amount are expected to pay taxes, as per the existing tax slabs. While these taxes can

Unit 12: Deductions from total income Law

be harsh on the bank balance of a taxpayer, the government also provides certain provisions wherein one can save tax. Tax deductions can help one reduce the taxable income, lowering their overall tax liability and thereby helping them save on taxes. The deduction one is eligible for depends on many factors, with different limits set for different purposes. Through this article, one can go through comprehensive knowledge and facts about provisions related to Rebates and Reliefs allowed under the Act. In simple terms, rebate is deduction from income tax payable Here Income Tax Payable I= Tax Payable + Cess + Surcharge + Interest (if any) – TDS. Rebate is deduction from tax payable and not from taxable income. Aggregate amount of Rebate shall not exceed Income Tax Payable in any case

Keywords

Eligible issue of capitalA public company created and registered in India, or a public financial institution, must issue capital that is eligible if the full proceeds of the issue are used solely and exclusively for the purposes of the businesses listed in section 80IA (4).

DisabilityThe terms "disability" and "multiple disability" as used in sections 2(a), 2(c), and 2(h) of the National Trust for Welfare of Persons with Autism, Cerebral Palsy, Mental Retardation, and Multiple Disabilities Act, 1999, respectively, shall have the meanings ascribed to them in Section 2(i) of the Persons with Disabilities (Equal Opportunities, Protection of Rights, and Full Participation) Act, 1995.

Person with disability:A person who meets the definition of a "person with disability" under Section 2(f) of the Persons with Disabilities (Equal Opportunities, Protection of Rights and Full Participation) Act of 1995 or Section 2(j) of the National Trust for Welfare of Persons with Autism, Cerebral Palsy, Mental Retardation and Multiple Disabilities Act of 1999 is one who has at least 40% of one or more "disabilities," as determined by a medical professional. Blindness, limited vision, leprosy-cured, hearing impairment, locomotor disability, mental retardation, and mental disease are all examples of disability.

Medical authority:To certify "autism," "cerebral palsy," "multiple disabilities," "person with disability," and "severe disability" as defined in sections 2(a), 2(c), 2(h), 2(j), and 2(o) of the National Trust for Welfare of Pers., "medical authority" means the medical authority described in Section 2(p) of the Persons with Disabilities (Equal Opportunities, Protection of Rights and Full Participation) Act, 1995, or (i.e., specified hospital or institution.)

SelfAssessment

1. Deduction under section 80C in respect of life insurance premium, contribution to Provident fund etc. is allowed to
 - A. Any assessee
 - B. An Individual
 - C. an individual /HUF
 - D. an individual /HUF who is resident in India

2. Which of the following is covered under section 80D of the Income Tax Act 1961
 - A. Repayment of loan taken for higher education
 - B. medical treatment of handicapped dependant
 - C. medical insurance premium
 - D. reimbursement of medical expense.

3. The flat amount of deduction under section 80U is
 - A. Rs. 50,000 and Rs. 75,000
 - B. Rs. 75,000 and Rs.1,00,000
 - C. Rs. 75,000 and Rs.1,10,000
 - D. Rs. 75,000 to Rs. 1,25,000

4. Deduction under section 80 E can be claimed for interest on loan for
 - A. any course of higher education
 - B. only postgraduate courses
 - C. only graduate courses
 - D. Any course of study after passing the senior secondary examination or its equal and from any recognised school board or university

5. Maximum qualifying amount for deduction (Rs.) under section 80C is
 - A. 50,000
 - B. 1,10,000
 - C. 1,00,000
 - D. 1,50,000

6. Deduction under section 80D of the Income Tax Act 1961 can be claimed by
 - A. an individual and huf opted for section 115BAC of the Income Tax Act 1961
 - B. an individual and huf not opted for section 115BAC of the Income Tax Act 1961
 - C. all assessee
 - D. none of the above

7. In Income Tax Act 1961 deduction under section 80C to 80U cannot exceed
 - A. gross total income
 - B. total income
 - C. income from business or profession
 - D. income from house property.

8. Deduction can be claimed for amount deposited under sukanyasamridhi account under section of the Income Tax Act 1961
 - A. 80CC
 - B. 80 C
 - C. 80 D
 - D. 80 DD

9. Chapter VIA of income tax at 1961 deals with
 - A. Deductions
 - B. exemptions
 - C. carry forward of losses
 - D. none of the above

10. Donation on PM's national Relief Fund is deductible 100% out of the gross total income of the assessee under section of the Income Tax Act 1961:
 - A. 80CC
 - B. 80 C
 - C. 80 D
 - D. 80 DD

11. REBATE OF INCOME-TAX is allowed under section

Unit 12: Deductions from total income Law

- A. 80CC
B. 80 C
C. 87A
D. 80 DD
12. RELIEF WHEN SALARY IS PAID IN ARREARS OR IN ADVANCE is allowed under section
- A. 80CC
B. 80 C
C. 89
D. 80 DD
13. Deduction in respect of employment of new workmen is allowed under section
- A. 80CC
B. 80 C
C. 80TTA
D. 80 DD
14. Deduction in case of a person with disability is allowed under section
- A. 80CC
B. 80 C
C. 80 TTA
D. 80 DD
15. Deduction in respect of contributions given by companies to political parties is allowed under section
- A. 80CC
B. 80 C
C. 80 GGB
D. 80 DD

Answers for Self Assessment

1. D 2. C 3. D 4. D 5. D
6. B 7. A 8. B 9. A 10. B
11. C 12. C 13. C 14. C 15. C

Review Questions

1. Briefly describe the relief provided by Section 89.
2. Briefly describe the deduction for the assessee's medical insurance premium.
3. Write a brief note on: a. The deduction for royalties from patents under section 80RRB.
4. Write a brief remark about: a. The deduction for authors' royalties under section 80QQB
5. Write a brief comment about: a. The deduction under section 80TTA for interest on savings account deposits.



Further Readings

- https://www.icsi.edu/media/webmodules/16112021_Advance_Tax_Laws.pdf
- Income Tax Law & Practice A.Y 2021-22 by Dr H.C. Mehrotra and Dr. S. P. Goyal. Sahitya Bhawan Publications
- Study Material on Direct Tax Laws and International Taxation by ICAI
- Direct Tax Laws and Practice by Dr. Girish Ahuja & Dr. Ravi Gupta
- <https://www.incometaxindia.gov.in/Charts%20%20Tables/Deductions.htm>

Unit 13: Assessment of individuals

CONTENTS

Objectives

Introduction

13.1 Computation of Total Income

13.2 Rounding-off Of Total Income [Sec. 288a]

13.3 Computation of Tax liability

Summary

Keywords

Self Assessment

Answers for Self Assessment

Review Questions

Further Readings

Objectives

After studying this unit, you will be able to:

- understand the computation of Total Income After Set-off of Losses Less Deductions Under Sections 80C to 80U
- understand the Computation of Tax Liability
- understand the concept of rounding off of Income and Tax.

Introduction

Every assessee who generates income during a Financial Year (FY) beyond the basic exemption limit is required to provide a statement detailing their earnings, deductions, and other pertinent data. The term for this is the Income Tax Return (ITR). The Income Tax Department will process your income tax returns once you, the taxpayer, file them. There are times when an assessee's return is chosen for an assessment based on criteria established by the Central Board of Direct Taxes (CBDT). The amount of income tax due is decided by the assessee. Different forms for filing an income tax return are available from the tax department. The assessee combines all of his sources of income and subtracts any losses, deductions, or exemptions he may have been eligible for during the year. The assessee's total income is then calculated. To calculate the tax due on such income, the assessee subtracts the TDS and advance tax from the total. Self assessment tax, if it is still owed by him, must be paid before he submits his income tax return. Self assessment is the name of this procedure.

13.1 Computation of Total Income

Illustration 1

- Municipal taxes paid by Mr Siddhant 4,300 (per annum)
- House Insurance 860
- He earned 2,700 in the share speculation business and lost 4,200 in the cotton speculation business.
- In 2016-17, he gifted 30,000 to his wife and 20,000 to his son, aged 11.

- The gifted amounts were advanced to Mr Rajesh, paying interest@19% per annum.
- Siddhant received a gift of 30,000 each from four friends.
- He contributed 50,000 to Public Provident Fund.
- Siddhant purchased a flat in a co-operative housing society in Delhi for 4,75,000 in April 2015, which was financed by
 - a loan from Life Insurance Corporation of India of 1,60,000@15% interest, his savings of 65,000 and
 - a deposit from a nationalized bank for 2,50,000 to whom this flat was given on lease for ten years. The rent payable by the bank was 3,500 per month. The following particulars are relevant:

Solution

Particulars	
Salary including dearness allowance	3,35,000
Bonus	11,000
Salary of servant provided by the employer	12,000
Rent paid by Siddhant for his accommodation	49,600
Bills paid by the employer for gas, electricity and water provided free of cost at the above flat	11,000

Income Under the Head Salaries

Salary Income		
Salary including dearness allowance		3,35,000
Bonus		11,000
Value of perquisites:		
(i) Salary of servant	12,000	
(ii) Free gas, electricity and water	11,000	23,000
		3,69,000
Less: Standard deduction under section 16(ia)		50,000
		319,000

Income Under the Head House Property

Income from house property	
----------------------------	--

Gross Annual Value (GAV) (Rent receivable is taken as GAV in the absence of other information) (3,500 × 12)	42,000
Less: Municipal taxes paid	4,300
Net Annual Value (NAV)	37,700
Less: Deductions under section 24	
(i) 30% of NAV	
(ii) Interest on loan from LIC @15% of	
1,60,000 [See Note 2]	35,310
	2390

Income under the head Profits and Gains from Business or Profession

Income from speculative business

Income from share speculation business	2,700	
Less: Loss of 4,200 from cotton speculation business set-off to the extent of 2,700	2,700	Nil

- Balance loss of 1,500 from cotton speculation business has to be carried forward to the next year as it cannot be set off against any other head of income.

Income from Other Sources

(i) Income on account of interest earned from advancing money gifted to his minor son is includible in the hands of Siddhant as per section 64(1A)	3,800	
Less: Exempt under section 10(32)	1,500	2,300
(ii) Interest income earned from advancing money gifted to wife has to be clubbed with the income of the assessee as per section 64(1)		5,700
(iii) Gift received from four friends (taxable under section 56(2)(x) as the aggregate amount received during the year exceeds 50,000)		1,20,000
Income from other sources		1280000

Total Income

Gross Total Income		4,49,390
Less: Deduction under section 80C		
Contribution to Public Provident Fund		50,000
Total Income		3,99,390

- It is assumed that the entire loan of ₹ 1,60,000 is outstanding as on 31.3.2023;
- Since Siddhant's own flat in a co-operative housing society, which he has rented out to a nationalized bank, is also in Delhi, he is not eligible for deduction under section 80GG in respect of rent paid by him for his accommodation in Delhi, since one of the conditions to be satisfied for claiming deduction under section 80GG is that the assessee should not own any residential accommodation in the same place.

13.2 Rounding-off Of Total Income [Sec. 288a]

The total income so computed will have to be rounded off to the nearest multiple of ₹ 10, i.e., if the last figure in the 'rupee element' is ₹ 5 or more, it should be rounded off to the next higher amount, which is a multiple of ₹ 10.

The 'paise' element should be ignored.

Example

Thus, if the total income works out to ₹ 41,645, it should be rounded off to ₹ 41,650, but if it works out to ₹ 41,644.98, it should be rounded off to ₹ 41,640.

The tax calculated on the total income should be rounded off to the nearest ₹ 10.

Amount of tax (including TDS or advance tax), interest, penalty, etc., and refund shall be rounded off to the nearest ₹ 10.

Example

- Tax liability actually worked out (₹): 4,876.49
- Tax liability as rounded off (₹): 4,880

Example

- Tax liability actually worked out (₹): 6,452.50
- Tax liability as rounded off (₹): 6,450

Example

- Tax liability actually worked out (₹): 8,738.92x
- Tax liability as rounded off (₹): 8,740

Example

- Tax liability actually worked out (₹): 5,132.75
- Tax liability as rounded off (₹): 5,130

Illustration

- During the previous year, Shri Prajapati received from his employer ₹ 2,00,000 as gratuity, out of which ₹ 1,10,000 is exempt u/s 10.
- His relevant data for the last few previous years are as follows:

Particulars	P.Y.2021-22
-------------	-------------

Basic	3,46,000
Taxable Gratuity	90,000
Gross salary	4,36,000
Less: Standard Deduction	50,000
Taxable Salary	3,86,000

Total Income

Taxable Salary	3,86,000
Income from house property	1,16,000
Gross total income	5,02,000
Less: Deduction	
Total income	5,02,000

Total income	5,02,000
Tax on above	12,900
Less: Rebate u/s 87A	Nil
Tax after Rebate	12,900

Add: Cess	516
Tax liability	13,416

Particulars	PY 19-20	PY 18-19	PY 17-18
Basic	2,75,000	1,70,000	65,000
Taxable Gratuity	30,000	30,000	30,000
Gross salary	3,05,000	2,00,000	95,000
Less: Standard Deduction	50,000		
Taxable Salary	2,55,000	2,00,000	95,000

Total Income

Taxable Salary	2,55,000	2,00,000	95,000
Income from house property	1,15,000	1,10,000	-65000
Gross total income	3,70,000	3,10,000	30000
Less: Deduction			
Total income	3,70,000	3,10,000	30000

Tax Liability

Unit 13: Assessment of Individuals

Total income	3,70,000	3,10,000	30000
Tax on above	6,000	3,000	Nil
Less: Rebate u/s 87A	6,000	3,000	Nil
Tax after Rebate	NIL	NIL	NIL
Add: Cess	NIL	NIL	NIL
Tax liability	NIL	NIL	NIL

Computation of Relief U/S 89 and Tax Liability For A.Y.2022-23

Particulars	Amount	Amount
Tax liability after cess but before relief u/s 89		13,416
Less: Relief u/s 89		(2,403)
Tax on taxable gratuity @ Average rate of tax of P.Y.2020-21 (90,000 * 2.67%)	2,403	
Tax on taxable gratuity @ Average of average tax of last 3 P.Y. (90,000 * 0.00%)	0	
Tax liability (Rounded off u/s 288B)		11,010

Relief When Payment is in the Nature of Taxable Gratuity

Where past services extend over a period of fifteen years

1. Calculate total income and tax liability considering taxable gratuity of the relevant previous year.
2. Calculate total income and tax on total income in respect of each of the three previous years immediately preceding the relevant previous year, adding 1/3rd of the taxable gratuity in each of the three years.
3. Calculate the average rate of tax for each year the average rate of tax (in %) = Tax, surcharge, and cess after a rebate of the respective year * 100 / Total Income
4. Calculate the average of "average rate of tax" of 3 previous years immediately preceding the relevant previous year.
5. Calculate tax on taxable gratuity by applying the average rate of tax of the relevant previous year.

6. Calculate tax on taxable gratuity by applying an average of the average rate of tax (as computed in step 4)
7. Relief u/s 89 = Tax as per Step 5 - Tax as per Step 6

Illustration

Particulars	Regular Tax Regime	New Tax
Business Income	1500000	1500000
Interest on SB Deposit	12000	12000
Interest on PPF	Exempt	Exempt
Gross Total Income	1512000	1512000

Calculation of Total Income

Particulars	Regular Regime	Tax	New Tax
Gross Total Income	1512000		1512000
Less: Deduction			
U/s 80C PPF Contribution	150000		NA
U/s 80TTA	10000		NA
Total Income	1352000		1512000

Tax

Total Income	1352000	1512000
Tax on Above	218100	191100
Less: Rebate u/s 87A	NA	NA
Tax after rebate	218100	191100
Add: Surcharge	Nil	Nil
Tax and Surcharge	218100	191100

Rounding off of tax

Tax and Surcharge	218100	191100
Add: HEC	8724	7644
Tax Liability	226820	198740
Round off u/s 288B		

Illustration

Particulars	
Income from house property	57,820

Profit and gains of business or profession	9,20,200
Income from other sources	33,924
Gross Total Income	10,11,944

Particulars	
Gross Total Income	1011944
Less: Deductions Under Chapter VI-A	10000
Total Income	1001944
Total Income (Rounded Off)	1001940

Total Tax liability

Total Income (rounded off)	1001940	
Tax on total income		
Upto 2,50,000	NIL	
2,50,001 - 5,00,000 @5%	12500	
5,00,001 - 10,00,000 @20%	100000	
10,00,001 - 10,01,940 @ 30%	582	113082
Add:Health and Education cess @ 4%		4523
Total tax liability		117605

Tax Payable (rounded off)

Total tax liability		117605
Less: Advance tax paid		70000
Less: Tax deducted at source on dividend income from an Indian Company u/s 194	1052	
Tax deducted at source on income from UTI u/s 194K	760	1812
Tax Payable		45793
Tax Payable (rounded off)		45790

Computation of Tax Payable in Accordance With the Provisions of Section 115BAC

Particulars	
Gross Total Income	10,11,944
Less: Deductions under Chapter VI-A [No deduction is allowable under Chapter VI-A, by virtue of section 115BAC(2)]	NIL
Total Income	10,11,944
Total Income (rounded off)	10,11,940

Total tax liability

Total Income (rounded off)	1011940	
Tax on total income		
Upto 2,50,000	NIL	

2,50,001 - 5,00,000 @5%	12500	
5,00,001 - 7,50,000 @10%	25000	
7,50,001 - 10,00,000 @15%	37500	
10,00,001 - 10,11,940 @ 20%	2388	77388
Add: Health and Education Cess @ 4%		3096
Total tax liability		80484

Tax Payable (rounded off)

Total tax liability		80484
Less: Advance tax paid		70000
Less: Tax deducted at source on dividend income from an Indian Company u/s 194	1052	
Tax deducted at source on income from UTI u/s 194K	760	1812
Tax Payable		8672
Tax Payable (rounded off)		8670

13.3 Computation of Tax liability

Example

Total Income	399390
Basic Exemption	250000

Taxable Total Income	149390
Tax 1,49,390@5%	7,470
Less: Rebate u/s 87A, since total income does not exceed ` 5,00,000	7,470
Tax liability	Nil

Illustration

Municipal taxes paid by Mr. Siddhant 4,300 (per annum)

House Insurance 860

He earned 2,700 in the share speculation business and lost 4,200 in the cotton speculation business.

In 2016-17, he gifted 30,000 to his wife and 20,000 to his son, aged 11. The gifted amounts were advanced to Mr. Rajesh, paying interest@19% per annum.

Siddhant received a gift of 30,000 each from four friends. He contributed 50,000 to Public Provident Fund.

Siddhant purchased a flat in a co-operative housing society in Delhi for 4,75,000 in April 2015,

- which was financed by a loan from Life Insurance Corporation of India of 1,60,000@15% interest,
- his savings of 65,000 and
- a deposit from a nationalized bank for 2,50,000 to whom this flat was given on lease for ten years. The rent payable by the bank was 3,500 per month. The following particulars are relevant:

Solution

Particulars	
Salary including dearness allowance	3,35,000
Bonus	11,000
Salary of servant provided by the employer	12,000
Rent paid by Siddhant for his accommodation	49,600
Bills paid by the employer for gas, electricity and water provided free of cost at the above flat	11,000

Income under the head salaries

Salary Income		
Salary including dearness allowance		3,35,000
Bonus		11,000

Value of perquisites:		
(i) Salary of servant	12,000	
(ii) Free gas, electricity and water	11,000	23,000
		3,69,000
Less: Standard deduction under section 16(ia)		50,000
		319000

Income Under the Head House Property

Income from house property	
Gross Annual Value (GAV) (Rent receivable is taken as GAV in the absence of other information) (3,500 × 12)	42,000
Less: Municipal taxes paid	4,300
Net Annual Value (NAV)	37,700
Less: Deductions under section 24	
(i) 30% of NAV	
(ii) Interest on loan from LIC @15% of 1,60,000 [See Note 2]	35,310
	2390

Income under the head Profits and Gains from Business or Profession

Income from speculative business

Income from share speculation business	2,700	
Less: Loss of 4,200 from cotton speculation business set-off to the extent of 2,700	2,700	Nil

- Balance loss of 1,500 from cotton speculation business has to be carried forward to the next year as it cannot be set off against any other head of income.

Income from Other Sources

(i) Income on account of interest earned from advancing money gifted to his minor son is includible in the hands of Siddhant as per section 64(1A)	3,800	
Less: Exempt under section 10(32)	1,500	2,300

(ii) Interest income earned from advancing money gifted to wife has to be clubbed with the income of the assessee as per section 64(1)	5,700
(iii) Gift received from four friends (taxable under section 56(2)(x) as the aggregate amount received during the year exceeds 50,000)	1,20,000
Income from other sources	1280000

Total Income

Gross Total Income	4,49,390
Less: Deduction under section 80C	
Contribution to Public Provident Fund	50,000
Total Income	3,99,390

- It is assumed that the entire loan of 1,60,000 is outstanding as on 31.3.2023;
- Since Siddhant's own flat in a co-operative housing society, which he has rented out to a nationalized bank, is also in Delhi, he is not eligible for deduction under section 80GG in respect of rent paid by him for his accommodation in Delhi, since one of the conditions to be satisfied for claiming deduction under section 80GG is that the assessee should not own any residential accommodation in the same place.

Summary

Although the terms Total Income (TI) and Gross Total Income (GTI) are interchangeable, they have different meanings in actuality. Where the total of all five heads of income is added up to determine gross total income. Total income is calculated after subtracting deductions under Sections 80C to 80U (or Chapter VI A deductions) of the Income Tax Act of 1961 from Gross Total Income. This indicates that GTI is a significant component from which we can derive TI by deducting a specific amount.

Keywords

Total Income:

Sum up your annual income under all the five heads of income and account for the deductions under chapter VIA. The net result would be your total or net income

Gross Income

Gross income is the aggregate income and a wider term from which total income can be arrived at after subtracting the deductions under section 80C to 80U of the income tax act.

Rounding off of total income: Rounding up the total income to the nearest multiple of Rs. is required. Any Paise shall be disregarded for this reason, and if the last digit is five or greater, the sum shall be rounded to the highest multiple. The final digit will be rounded off to the next lower multiple if it is less than 5.

Self Assessment

1. In case of an Individual (resident or non-resident) (Other than senior and super senior citizen), Rate of Income-tax for the Assessment Year 2022-23 for the net income range Up to Rs. 2,50,000 is
 - A. Nil
 - B. 5
 - C. 20
 - D. 30

2. In case of an Individual (resident or non-resident) (Other than senior and super senior citizen), Rate of Income-tax for the Assessment Year 2022-23 for the net income ranges from Rs. 2,50,000 to Rs. 5,00,000 is
 - A. Nil
 - B. 5
 - C. 20
 - D. 30

3. In case of an Individual (resident or non-resident) (Other than senior and super senior citizen), Rate of Income-tax for the Assessment Year 2022-23 for the net income ranges from Rs. 5,00,000 to Rs. 10,00,000 is
 - A. Nil
 - B. 5
 - C. 20
 - D. 30

4. In case of an Individual (resident or non-resident) (Other than senior and super senior citizen), Rate of Income-tax for the Assessment Year 2022-23 for the net income Above Rs. 10,00,000 is
 - A. Nil
 - B. 5
 - C. 20
 - D. 30

5. In case of an Individual (resident or non-resident) (who is 60 years or more at any time during the previous year), Rate of Income-tax for the Assessment Year 2022-23 for the net income range Up to Rs. 3,00,000 is
 - A. Nil
 - B. 5
 - C. 20
 - D. 30

6. In case of an Individual (resident or non-resident) (Who is 80 years or more at any time during the previous year), Rate of Income-tax for the Assessment Year 2022-23 for the net income range Up to Rs..... is Nil.
 - A. 2,50,000
 - B. 3,00,000

-
- C. 3,50,000
D. 5,00,000
7. In case of an Individual (resident or non-resident) (who is 80 years or more at any time during the previous year), Rate of Income-tax for the Assessment Year 2022-23 for the net income ranges from Rs. 5,00,000 to Rs. 10,00,000 is
- A. Nil
B. 5
C. 20
D. 30
8. Surcharge is levied on the amount of income-tax at following rates if total income of an assessee ranges Rs. 50 Lakhs to Rs. 1 Crore:
- A. 10%
B. 15%
C. 25%
D. 37%
9. Surcharge is levied on the amount of income-tax at following rates if total income of an assessee ranges from Rs. 1 Crore to Rs. 2 Crore:
- A. 10%
B. 15%
C. 25%
D. 37%
10. Surcharge is levied on the amount of income-tax at following rates if total income of an assessee ranges Rs. 2 Crores to Rs. 5 Crore:
- A. 10%
B. 15%
C. 25%
D. 37%
11. Surcharge is levied on the amount of income-tax at following rates if total income of an assessee ranges Rs. 5 crores to Rs. 10 Crores:
- A. 10%
B. 15%
C. 25%
D. 37%
12. The maximum rate of surcharge on tax payable on income chargeable to tax under [sections 111A, 112A and 115AD](#) is
- A. 10%
B. 15%
C. 25%
D. 37%

13. Health and Education Cess is levied at the rate of% on the amount of income-tax plus surcharge.
- A. 1
B. 2
C. 3
D. 4
14. A resident individual (whose net income does not exceed Rs.) can avail rebate under [section 87A](#).
- A. 2,50,000
B. 3,00,000
C. 3,50,000
D. 5,00,000
15. Under Special tax Rate for Individual and HUFs, the Finance Act, 2020, has provided an option to Individuals and HUF for payment of taxes at the following rate for total income exceeding Above 15,00,000.
- A. 10%
B. 15%
C. 20%
D. 30%

Answers for Self Assessment

1	A	4	D	7	C	10	C	13	D
2	B	5	A	8	A	11	D	14	D
3	C	6	D	9	B	12	B	15	D

Review Questions

1. Why is the Total Income (TI) calculation significant under the Income Tax Act?
2. What is Total Income and How it is Calculated?
3. What distinguishes gross income from total income?
4. What distinguishes total income from taxable income?
5. How do you assess the tax liability of an individual?

**Further Readings**

- https://www.icsi.edu/media/webmodules/16112021_Advance_Tax_Laws.pdf
- Income Tax Law & Practice A.Y 2021-22 by Dr H.C. Mehrotra and Dr. S. P. Goyal. Sahitya Bhawan Publications
- Study Material on Direct Tax Laws and International Taxation by ICAI
- Direct Tax Laws and Practice by Dr. Girish Ahuja & Dr. Ravi Gupta

Unit 14: Introduction to Basic Concepts of Income Tax Law**CONTENTS**

Objectives

Introduction

14.1 Permanent Account Number

14.2 Importance of PAN

14.3 What is TDS? - TDS Meaning and Full Form

14.4 Filing of Return

Summary

Keywords

Self Assessment

Answers for Self Assessment

Review Questions

Further Readings

Objectives

After studying this unit, you will be able to:

- understand the concept of PAN and related provisions.
- understand the concept of TDS
- understand the concept of Return of Income.
- identify the persons who are compulsorily required to file returns.
- know the consequences of non-filing or delayed filing of returns.

Introduction

PAN gives the department the ability to recognize and associate all of the PAN holder's transactions with the department. These transactions cover things like tax payments, TDS/TCS credits, income returns, certain transactions, correspondence, etc. It makes it simple to match up different investments, borrowings, and other commercial operations of PAN holders as well as easily retrieve information about PAN holders. Income Tax Return is referred to as ITR, the assesses declaration of income and any associated taxes in the format required by law. It is a regulated form that is used to inform the Income-tax Department of the specifics of an individual's income received during a financial year and the taxes that were paid on that income. Additionally, it permits the carry forward of losses and an income tax department refund claim.

14.1 Permanent Account Number

Permanent Account Number (PAN) is an alpha-numeric (ten characters) code given to a person by the income tax department for the purpose of identification of the assessee. A person can have only one PAN.

How PAN is formed and how it gets its unique identity?

- PAN is a ten-digit unique alphanumeric number issued by the Income Tax Department.
- The formation of PAN is discussed below:

- Out of the first five characters, the first three represent the alphabetic series running from AAA to ZZZ. (E.g., ALWPG5809L).
- The fourth character of PAN represents the status of the PAN holder (E.g., ALWPG5809L).
 - “A” stands for Association of Persons (AoP)
 - “B” stands for Body of Individuals (BOI)
 - “C” stands for Company
 - “F” stands for Firm/Limited Liability Partnership
 - “G” stands for Government Agency
 - “H” stands for Hindu Undivided Family (HUF)
 - “J” stands for Artificial Juridical Person
 - “L” stands for Local Authority
 - “P” stands for Individual
 - “T” stands for Trust
- Fifth character of PAN represents the first character of the PAN holder’s last name/surname in the case of an individual.
- In the case of non-individual PAN holders, the fifth character represents the first character of the PAN holder’s name (E.g., ALWPG5809L) Next four characters are sequential numbers running from 0001 to 9999 (E.g., ALWPG5809L).
- The Last character, i.e., the tenth character, is an alphabetic check digit (E.g., ALWPG5809L).
- The combination of all the above items gives the PAN its unique identity.

Allotment of Pan

A. On Application

B. Suo-moto allotment of PAN

A. On Application

Compulsory application for allotment of PAN as per sec. 139A & rule 114, the following persons are under statutory obligation to apply for PAN

Who has to obtain PAN?

PAN is to be obtained by following persons:

- Every person if his total income or the total income of any other person in respect of which he is assessable during the previous year exceeds the maximum amount which is not chargeable to tax.
- A charitable trust who is required to furnish a return under Section 139(4A)
- Every person who is carrying on any business or profession whose total sale, turnover, or gross receipts are or is likely to exceed five lakh rupees in any previous year
- Every person who intends to enter into specified financial transactions in which quoting of PAN is mandatory

Penalty for failure to apply for PAN

- Failure to apply for PAN or to quote PAN in prescribed documents (discussed later in this chapter) attracts a penalty of 10,000 u/s 272B.

Voluntary application for allotment of PAN [Sec. 139A(3)]

- The section empowers a person to apply for a PAN, even though the person does not fall under any of the categories mentioned above.
- However, a person, who has already been allotted a PAN under the new series, shall not apply for another PAN.

Interchangeability of PAN and Aadhar [Sec. 139A(5E)]

- Every person who is required to furnish or intimate or quote his PAN, and who, --
 - a. has not been allotted PAN but possesses the Aadhaar number, may furnish or intimate or quote his Aadhaar number in lieu of the PAN, and such person shall be allotted a PAN in such manner as may be prescribed;
 - b. has been allotted a PAN, and who has intimated his Aadhaar number in accordance with provisions of sec. 139AA, may furnish or intimate or quote his Aadhaar number in lieu of the PAN

Whom to apply (either compulsory or voluntary)

- The application is to be made to the Assessing Officer or any other person assigned the function of allotment of PAN.
- However, where no such Assessing Officer or other person has been assigned such function, the application shall be made to the Assessing Officer having jurisdiction over the person.

Form of application¹ – The prescribed forms are as under

- For Indian Citizen / Indian Company / Entities incorporated in India / Unincorporated entities formed in India: 49A
- In other cases: 49AA

B. Suo-moto allotment of PAN

As per sec 139A(1B), for the purpose of collecting any information which may be useful for the purposes of the Act, the Central Government may, by way of a notification, specify any class of person to apply within the prescribed time to the AO for allotment of PAN.

- Section 139A(2) empowers the Assessing Officer to allot a PAN to any person other than the person falling under the categories mentioned above.

14.2 Importance of PAN

- PAN or Aadhar Number must be quoted in all documents and challans [Sec. 139A(5)]
- PAN or Aadhar Number must be quoted in documents pertaining to certain prescribed transactions [Sec. 139A(5)(c) & Rule 114B]

PAN or Aadhar Number must be quoted in all documents and challans [Sec. 139A(5)]

- a. A person to whom a PAN or Aadhar is allotted is required to quote that number in –
 - All his returns to; or
 - Any correspondence with; or
 - Any other documents to,
 - Income-tax authority-
- b. A person to whom a PAN or Aadhar is allotted is required to quote that number in challans for payment of any sum due under this Act

PAN or Aadhar Number must be quoted in documents pertaining to certain prescribed transactions [Sec. 139A(5)(c) & Rule 114B]

Every person shall quote its PAN or Aadhar in all documents pertaining to following transactions entered into by him –

1. Transactions relating to sale or purchase of a motor vehicle (other than two wheeled vehicles), which requires registration.
2. Opening an account [other than a time-deposit and a Basic Savings Bank Deposit Account] with a banking company or a cooperative bank

3. Making application for the issue of a credit card or debit card.
4. Opening of a Demat account
5. Payment in cash exceeding 50,000 to a hotel or restaurant against a bill or bills at any one time
6. Payment in cash exceeding 50,000 in connection with travel to any foreign country or payment for the purchase of any foreign currency at any one time
7. Payment exceeding 50,000 to any mutual fund for the purchase of its units.
8. Payment exceeding 50,000 to a company or an institution for acquiring debentures or bonds issued by it
9. Payment exceeding 50,000 to RBI for acquiring bonds issued by it.
10. Deposit in cash exceeding 50,000 during any one day with a banking company or a cooperative bank
11. Purchase of bank drafts or pay orders or banker's cheques from a banking company or a co-operative bank in cash for an amount exceeding 50,000 during any one day
12. A time deposit of an amount exceeding 50,000 or aggregating to more than 5 lakh during a financial year with (i) a banking company or a co-operative bank; or (ii) a Post Office; or (iii) a Nidhi referred to in section 406 of the Companies Act, 2013; or (iv) a non-banking financial company
13. Payment in cash or by way of a bank draft or pay order or banker's cheque of an amount aggregating to more than 50,000 in a financial year for one or more pre-paid payment instruments, as defined in the policy guidelines for issuance and operation of pre-paid payment instruments issued by Reserve Bank of India u/s 18 of the Payment and Settlement Systems Act, 2007, to a banking company or a co-operative bank
14. Payment aggregating to more than 50,000 in a financial year as life insurance premium to an insurer
15. A contract for sale or purchase of securities (other than shares) where transaction value exceeds 1 lakh
16. Sale or purchase, by any person, of shares of a company not listed in a recognised stock exchange where transaction value exceeds 1 lakh
17. Sale or purchase of any immovable property where the amount exceeds 10 lakh or stamp value exceeds 10 lakh
18. Sale or purchase, by any person, of goods or services of any nature other than those specified above where transaction value exceeds 2 lakh

PAN or Aadhar Number on TDS & TCS Certificate

(a) On TDS: Every person is required to intimate his PAN to the person who has deducted the tax at the source [Sec. 139A(5A)].

Exceptions: This provision is not applicable to an assessee who furnishes to the payer a declaration in writing in the prescribed form (Form 15G or 15H) and manner to the effect that the tax on his estimated total income is nil.

- The person deducting tax at source is required to quote -
 - PAN of the payee;
 - PAN of himself;
 - Tax Deduction Account Number (TAN) of himself,

- in all statements, certificates furnished u/s 200(3) or 203 or 206 [Sec. 139A(5B)].

(b) Every person responsible for collecting tax under sec.206C shall quote the PAN of every buyer, licensee, or lessee in all certificates furnished in accordance with Sec. 206C(3) or 206C(5) and in all returns prepared u/s 206C(5A)/(5B) to the Income-tax authority [Sec. 139A(5D)]

Unit 14: Introduction to Basic Concepts of Income Tax Law

Every buyer, licensee, or lessee must intimate his PAN to the seller who has collected the tax at the source [Sec. 139A(5C)]

Intimation for Any Change

- Every person shall intimate the Assessing Officer, in the prescribed manner, any change in his address or the name & nature of his business based on which PAN was allotted to him [Sec. 139A(5)(d)]

How does Income Tax Department ensure that PAN is quoted on transactions in which quoting of PAN is mandatory?

- Thus, the receiver of the document relating to economic or financial transactions notified by the Central Board of Direct Taxes (CBDT) will ensure that PAN is quoted in the respective document.

Can I file my return of income without quoting PAN?

- It is mandatory to quote PAN on the return of income.
- With effect from September 1, 2019, an assessee can file his return of income by quoting his Aadhaar number instead of quoting PAN.

Is it mandatory to link Aadhaar number with PAN?

- The Finance Act, 2017 had inserted a new Section 139AA in the Income-tax Act, 1961, requiring every person who is eligible to obtain Aadhaar to quote his Aadhaar number while applying for PAN or furnishing return of income with effect from July 1, 2017.

Instant PAN

- Income-tax Dept. has launched a new functionality on the e-filing portal, which allots a PAN to the assessee on the basis of his Aadhaar Number.

This facility can be used by an assessee only if the following conditions are fulfilled:

- a. He has never been allotted a PAN;
- b. His mobile number is linked with his Aadhaar number;
- c. His complete date of birth is available on the Aadhaar card; and
- d. He should not be a minor on the date of application for PAN

How to Get Instant PAN Using This Functionality?

1. Goto <https://eportal.incometax.gov.in/iec/fooservices/#/pre-login/instant-e-pan> and click on "Get New e-PAN"

2. Enter your 12 digit Aadhaar number for PAN allotment and click on continue.
3. Enter the OTP received on the mobile number linked with the Aadhaar No. to validate the Aadhaar details.
4. Enter other details and submit to get the e-PAN.

Through NSDL Portal:

The government has made provisions for applicants to apply for PAN through the Income Tax PAN Services Unit of NSDL. Follow these easy steps to apply for a PAN online:

Step1: Open the NSDL site

(<https://www.onlineservices.nsd.com/paam/endUserRegisterContact.html>) to apply for a new PAN.

Step 2: Select the Application type - New PAN for Indian citizens, foreign citizens or for change/correction in existing PAN data.

Step 3: Select your category - individual, associations of persons, a body of individuals, etc.

Step 4: Fill in all the required details like name, date of birth, email address and your mobile number in the PAN form.

Step 5: On submitting the form, you will get a message regarding the next step.

Step 6: Click on the "Continue with the PAN Application Form" button.

Step 7: You will be redirected to the new page where you have to submit your digital e-KYC.

Step 8: Select whether you need physical PAN card or not and provide the last four digits of your Aadhaar number.

Step 9: Enter your personal details, contact and other details in the next part of the form

Step 10: Enter your area code, AO Type and other details in this part of the form. You can also find these details in the tab below

Step 11: The last part of the form is the document submission and declaration.

Step 12: Enter the first 8 digits of your PAN card to submit the application. You will get to see your completed form. Click Proceed if no modification is required.

- Step 13: Select the e-KYC option to verify using Aadhaar OTP. For Proof of Identity, Address and Date of Birth, select Aadhaar in all fields and click on Proceed to continue.
- Step 14: You will be redirected to the payment section where you have to make payment either through demand draft or through net banking/debit/credit card.

Unit 14: Introduction to Basic Concepts of Income Tax Law

- Step 15: A payment receipt will be generated on successful payment. Click on Continue.
- Step 16: Now for Aadhaar Authentication, tick the declaration and select “Authenticate” option.
- Step 17: Click on “Continue with e-KYC” after which an OTP will be sent to the mobile number linked with Aadhaar.
- Step 18: Enter the OTP and submit the form.
- Step 19: Now click on “Continue with e-Sign” after which you will have to enter your 12-digit Aadhaar number. An OTP will be sent to the mobile number linked with Aadhaar.
- Step 20: Enter OTP and submit the application to get the Acknowledgement slip in pdf having your date of birth as the password in DDMMYYYY format.

Through UTIITSL Portal:

Here is how you can apply for a new PAN card online through the UTIITSL website:

Step 1: Visit the UTIITSL website and under PAN Services select ‘PAN Card for Indian Citizen/NRI’

Step 2: Click on ‘Apply for New PAN Card (Form 49A)’

Step 3: Choose either the ‘Physical Mode’ whereby you will have to submit the printed-signed application form at the nearest UTIITSL office or the ‘Digital Mode’ whereby the application form is signed using Dsc mode or using Aadhaar based eSignature and you need not submit the physical copy for the form.

Step 4: Fill in your personal and other mandatory details

Step 5: Verify the correctness of the filled-in information and click on the ‘Submit’ button

Step 6: Upon verification, you can go ahead and make the payment online by choosing either of the available payment gateway options- BillDesk or PayU India. You can pay via net banking, debit card, credit card, cash card, etc.

Step 7: On successful payment, you will get a payment confirmation. You can either save this or take a printout of the same.

Step 8: Affix 2 passport size photographs (3.5×2.5 cms) on the printed form and put your signature on the space provided

Step 9: Attach a copy of your identity, address and date of birth proof documents along with your completely filled application form and submit online or send the same to the nearest UTIITSL office for processing and issuance of your PAN Card.

How to Correct Any Mistake in PAN Card or Intimate Any Change In Data Pertaining to PAN?

Request for reissue of lost PAN card or for change/correction in PAN data is to be filed in “Request for New PAN Card or/ And Changes or Correction in PAN Data.”

How to Correct Any Mistake in PAN Card or Intimate Any Change In Data Pertaining to PAN?

- For Changes or Corrections in PAN data, fill all mandatory fields of the Form and select the corresponding box on the left margin of the appropriate field where correction is required.
- If the application is for re-issuance of a PAN card without any changes in PAN-related data of the applicant, fill all fields in the Form but do not select any box on the left margin.

How to Correct Any Mistake in PAN Card or Intimate Any Change In Data Pertaining to PAN?

- In case of either a request for Change or Correction in PAN or a request for re-issuance of a PAN Card without any changes in PAN data, the address for communication will be updated in the ITD database using the address for communication provided in the application.

- For Cancellation of PAN, fill all mandatory fields in the Form, enter PAN to be cancelled in the appropriate column of the Form and select the check box on the left margin. PAN to be cancelled should not be the same as PAN (the one currently used) mentioned at the top of the Form

Holding of More than one PAN not Allowed

- A penalty of Rs. 10,000/- is liable to be imposed under section 272B of the Income-tax Act, 1961 for having more than one PAN.

How to Know PAN, If the PAN Card is Lost and PAN is Forgotten?

- In such a case, one can know his PAN by using the facility of "Know Your PAN" provided by the Income Tax Department. This facility can be availed of from the website of the Income Tax Department -
- www.incometaxindia.gov.in

How to Know PAN, If the PAN Card is Lost and PAN is Forgotten?

- A person can know his PAN online by providing his core details like Name, Father's Name, and Date of Birth. •Apply for a duplicate PAN card by submitting the "Request for New PAN Card or/ And Changes or Correction in PAN Data."

Linking of PAN with Aadhaar Number

- The Finance Act, 2017 had inserted a new section 139AA in the Income-tax Act, 1961, requiring every person who is eligible to obtain Aadhaar to quote his Aadhaar number while applying for PAN or furnishing a return of income with effect from July 1, 2017.
- Section 139AA further provides that every person who has been allotted PAN as on the 1st day of July 2017 and who is eligible to obtain an Aadhaar number shall intimate his Aadhaar number on or before 31-03-2022 to the Income-tax Department.
- In case of failure to intimate the Aadhaar number, PAN allotted to the person shall be made inoperative after the date so notified
- The CBDT has notified that all the consequences provided under the Income-tax Act for not furnishing, intimating, or quoting PAN shall come into effect from 01-04-2023 if PAN becomes inoperative due to non-linking of it with Aadhaar. However, the taxpayer is liable to pay the fee if PAN is linked with Aadhaar from 01-04-2022 to 31-03-2023

Consequences for not linking PAN with Aadhaar Number

- The Rule 114AAA(2) provides that where a person whose PAN has become inoperative, it shall be deemed that he has not furnished, intimated, or quoted the PAN, as the case may be, and he shall be liable for all the consequences under the Act for not furnishing, intimating or quoting the PAN.
- The Central Board of Direct Taxes has notified Rule 114AAA prescribing the manner and consequences if PAN becomes inoperative.
- However, the person can reactivate his PAN by subsequently intimating his Aadhaar to the Department

Fee For Default Relating To Intimation Of Aadhaar Number

- The Finance Act, 2021 has inserted a new Section 234H to levy a fee for default in intimating the Aadhaar Number. If a person is required to intimate his Aadhaar under Section 139AA and such person fails to do so, he shall be liable to pay a fee, as may be prescribed, not exceeding Rs. 1,000 at the time of making such intimation

Unit 14: Introduction to Basic Concepts of Income Tax Law

- The CBDT vide notification No. 17/2022, dated 29-03-2022, has amended Rule 114 to prescribe the fees to be levied if Aadhaar is not linked with PAN.
- As per Rule 114(5A), if a person intimates his Aadhaar number after the due date, then he shall be liable to pay a fee of:
 - a) Rs. 500, if such intimation is made between 01-04-2022 and 30-06-2022; and
 - b) Rs. 1,000, in all other cases.

How to Link Aadhaar Number With PAN?

The following modes have been prescribed to link Aadhaar number with PAN:

a. SMS:

Send SMS to 567678 or 56161 from your registered mobile number in the following format:
UIDPAN

For E.g., UIDPAN 123456789000 EPOPE1234E

b. Online:

By visiting the website of the PAN Service providers

(i.e., www.tin-nsdl.com or www.utiitsl.com).

Click on the button 'Link Aadhaar to PAN' which will direct you to the income-tax website.

By visiting directly, the e-filing website (i.e., www.incometaxindiaefiling.gov.in).

- c. Paper mode: File one-page Form along with a minimal fee with the designated PAN centre. Copies of PAN card and Aadhaar card are to be furnished.

Penalty for not Complying with Provisions Relating to PAN or Aadhar (Section 272B)

- Penalty shall be Rs. 10000 for each default.

As the Finance (No. 2) Act, 2019 has provided for interchangeability of Aadhar with PAN, Consequential amendments have been made in the penal provisions of Section 272B so as to levy a penalty of Rs. 10,000 for each default in the following cases:

- a. If the assessee fails to quote or intimate his PAN or Aadhaar or quotes or intimates invalid PAN or Aadhaar.
- b. If the assessee fails to quote or authenticate his PAN or Aadhaar in specified transactions.
- c. If the receiver (i.e., banks, financial institutions, etc.) of documents in respect of specified transactions fails to ensure that the PAN or Aadhaar are duly quoted and authenticated.

14.3 What is TDS? – TDS Meaning and Full Form

TDS or Tax Deducted at Source is income tax reduced from the money paid at the time of making specified payments such as rent, commission, professional fees, salary, interest etc., by the persons making such payments.

Usually, the person receiving income is liable to pay income tax.

- The incomerecipient receives the net amount (after reducing TDS).
- The recipient will add the gross amount to his income and the amount of TDS is adjusted against his final tax liability.
- The recipient takes credit for the amount already deducted and paid on his behalf.

When should TDS be deducted and by whom?

- Any person making specified payments mentioned under the Income Tax Act must deduct TDS when making such specified payment.

- But no TDS has to be deducted if the person making the payment is an individual or HUF whose books are not required to be audited.
- Investment proofs
- [Form 15G and Form 15H](#)

What is the Due Date For Depositing the TDS to the Government?

- The Tax Deducted at Source must be deposited to the government by the 7th of the subsequent month.

How to Deposit TDS?

- Tax Deducted at Source has to be deposited using Challan ITNS-281 on the government portal.

How and When to File TDS Returns?

Form No	Transactions reported in the return	Due date
Form 24Q	TDS on Salary	Q1 - 31st July Q2 - 31st October Q3 - 31st January Q4 - 31st May
Form No	Transactions reported in the return	Due date
Form 27Q	TDS on all payments made to non-residents except salaries	Q1 - 31st July Q2 - 31st October Q3 - 31st January Q4 - 31st May
Form No	Transactions reported in the return	Due date
Form 26QB	TDS on sale of property	30 days from the end of the month in which TDS is deducted

Form No	Transactions reported in the return	Due date
Form 26QC	TDS on rent	30 days from the end of the month in which TDS is deducted

What is a TDS Certificate?

Form	Certificate of	Frequency	Due date
Form 16	TDS on salary payment	Yearly	31st May

Unit 14: Introduction to Basic Concepts of Income Tax Law

Form 16 A	TDS on non-salary payments	Quarterly	15 days from due date of filing return
Form	Certificate of	Frequency	Due date
Form 16 B	TDS on sale of property	Every transaction	15 days from due date of filing return
Form 16 C	TDS on rent	Every transaction	15 days from due date of filing return

TDS Credits in Form 26AS

- TDS deductions are linked to PAN numbers for both the deductor and deductee.
- If TDS has been deducted from any of your income, you must go through the Tax Credit [Form 26AS](#).
- This form is a consolidated tax statement that is available to all PAN holders.
- Since all TDS is linked to your PAN, this form lists out the details of TDS deducted on your income by each deductor for all kinds of payments made to you – whether those are salaries or interest income – all TDS linked to your PAN is reported here.

SMS Alerts for Higher Transparency

- The income tax department has been sending SMS to the taxpayers from VK-ITDEFL that mentions the amount of tax deducted at source (TDS) against the taxpayer's PAN (Permanent Account Number).
- The amount of TDS would stand accumulated in your [Form 26AS](#) for the respective financial year.

Tax Liability in a Case Where TDS is Already Deducted from Income

- On salary, TDS is deducted based on your income tax slab.
- In the case of other income types, the TDS rates are fixed and vary between 10% and 20%.
- Separately, you would be required to calculate your annual income by aggregating income from all sources.
- Your actual tax liability would be calculated on the total taxable income.
- From the taxes calculated, you can claim credit for TDS deducted on your various receipts.
- Reduce the tax deducted at source from your actual tax liability to know the balance to be paid to the income tax department.

What is the Responsibility of the Person Deducting Tax at Source?

- Obtain the Tax Deduction Account Number and mention it in all the documents pertaining to TDS.
- Deduct the TDS at the applicable rate.
- Deposit the TDS amount with the Government within the specified due date.
- File TDS returns within the specified due date.
- Issue the TDS certificate to the payee within the specified due date.

At What Rate the Deductor Will Deduct TDS If I Do Not Furnish My Permanent Account Number To Them?

- Deductor shall deduct TDS at the higher of the rate prescribed in the relevant provisions of the Act or at 20%.

What is the Difference Between TAN and PAN?

- PAN is a Permanent Account Number and TAN stands for Tax Deduction Account Number.
- TAN should be obtained by the person responsible for deducting TDS, i.e., the deductor. The deductor is required to quote TAN in all the documents relating to TDS.

How Many Types of TDS are There?

- There are several types of TDS defined by the law.

TDS on Salary [Sec. 192]

- Who is responsible for deducting tax
 - Any person responsible for paying any income chargeable under the head "Salaries" (i.e., employer) is required to deduct tax at source.
- When tax shall be deducted
 - Tax shall be deducted at the time of payment of such income.
- Rate of TDS
 - Tax shall be deducted at the average rate of tax, computed on the basis of prescribed rates in force for the financial year in which payment to the employee is made.

TDS ON Payment from Employees Provident Fund [SEC. 192A]

- Who is responsible to deduct tax:
 - The trustees of the Employees' Provident Fund Scheme, 1952, framed u/s 5 of the Employees' Provident Funds and Miscellaneous Provisions Act, 1952 or any person authorized under the scheme to make payment of the accumulated balance due to employees.
- When tax shall be deducted:
 - At the time of making of payment.
- Tax is deducted on:
 - The accumulated balance due to an employee participating in a recognized provident fund includible in his total income owing to the not applicability of the provisions of rule 8 of Part A of the Fourth Schedule.
- Rate of TDS: 10%
 - Any person entitled to receive any amount on which tax is deductible shall furnish his Permanent Account Number (PAN) to the person responsible for deducting such tax, failing which tax shall be deducted at the maximum marginal rate
- When TDS is not applicable:
 - Aggregate amount of such payment to the payee is less than 50,000.

TDS on Interest on Securities [SEC. 193]

- Who is responsible to deduct tax:
 - Any person responsible for payment of interest on securities (other than interest on Government securities and certain specified securities) to any resident person.

Note: In the following cases tax is not required to be deducted:

1. Interest payable to a resident individual or a resident HUF on debentures is not subject to TDS provided the following conditions are satisfied –
 - a. Such debentures are issued by a company in which the public is substantially interested;
 - b. Such debentures may be listed or unlisted.
 - c. The interest is paid by the company by an account payee cheque.

Unit 14: Introduction to Basic Concepts of Income Tax Law

- d. The amount of such interest payable during the financial year to the such individual does not exceed 5,000.
2. Any interest payable on any security of the Central or State Government. (However, tax is required to be deducted on interest payable on 8% Savings (Taxable) Bonds, 2003 or 7.75% Savings (Taxable) Bonds, 2018, if the amount of interest in a financial year exceeds 10,000).
 3. Any interest payable on any security issued by a company, where such security is in dematerialised form and is listed on a recognised stock exchange.
 4. Any interest payable on securities beneficially held by Life Insurance Corporation of India or General Insurance Corporation of India, or any of the 4 companies formed by virtue of the scheme framed u/s 16(1) of the General Insurance Business (Nationalization) Act, 1972 or any other insurer.
 5. Any interest payable to Regimental Fund or non-Public Fund established by Armed Force [income of whose is exempt u/s 10(23AA)].

When tax shall be deducted:

At the time of payment or crediting the payee, whichever is earlier. Tax point: Where any amount is credited to any account (e.g. "Interest payable account" or "Suspense account") instead of the Payee account, such crediting shall be deemed to be the credit of such income to the account of the payee.

- Rate of TDS: 10% (No surcharge, health and education cess)

TDS on Dividends [SEC. 194] Amended

- Who is responsible for deducting tax: The principal officer of a domestic company paying dividend u/s 2(22) to any resident shareholder.
- When tax shall be deducted: At the time of payment
- Rate of TDS: 10% (No surcharge, health and education cess) on dividend considered u/s 2(22)

TDS on Interest Other Than Interest on Securities [SEC. 194A] Amended

Who is responsible to deduct tax

The following persons are responsible for deducting tax at source on interest other than interest on securities to a resident person -

- Any person, other than Individual or HUF; or
- An individual or a HUF whose total sales, gross receipts or turnover from the business or the profession carried on by him exceed 1 crore in case of business or 50 lakh in case of profession during the financial year immediately preceding the financial year in which such interest is credited or paid.
- Note: No tax shall be deducted at source if, during the financial year, interest payable by the payer to the payee does not exceed 5,000.

TDS on Winning from Lotteries or Cross Word Puzzles, Etc. [Sec. 194B]

- Who is responsible for deducting tax:
 - Any person responsible for paying to any person any income by way of winning from any lottery or crossword puzzle or card game and other game of any sort, exceeding 10,000.
- Tax point:
 - If income is more than 10,000 (say 12,000), then tax shall be deducted on the whole amount (i.e. 12,000).
- Rate of TDS:
 - 30% (in case of non-resident payee, applicable surcharge, health and education cess shall also be considered)

- Rate of TDS as a % of amount paid or payable
 - Resident Person: 30%
 - Non-Resident 30% + Surcharge + Health and Education cess.

TDS on Winning from Horse Races [Sec. 194BB]

- Who is responsible for deducting tax:
 - Any person responsible for paying to any person any income by way of winning from horse races, exceeding 10,000.
- Rate of TDS:
 - See sec. 194B (TDS on Winning from lotteries or cross word puzzles or card games, etc.)
- When tax shall be deducted: At the time of payment.

TDS on Payment to Contractor [SEC. 194C]

- Who is responsible for deducting tax
- Any specified person¹ responsible for paying any sum to any resident-contractor for carrying out any work (including supply of labour for carrying out any work) in pursuance of a contract.

When tax cannot be deducted

- Case 1 When following conditions are satisfied then tax cannot be deducted:
 - i. Any sum credited or paid in pursuance of any contract, the consideration for which does not exceed 30,000; and Tax point: The limit of 30,000 is on individual contract.
 - ii. Where the aggregate of the amounts of such sums credited or paid or likely to be credited or paid during the financial year does not exceed 1,00,000
 - Case 2 When the following conditions are satisfied, then tax cannot be deducted:
 - a. Amount is paid or payable to a resident contractor during the course of plying, hiring or leasing goods carriage (here-in-after referred to as transport operator).
 - b. Such operator furnishes his Permanent Account Number (PAN) to the payer.
 - c. Where such contractor owns 10 or fewer goods carriages at any time during the previous year and furnishes a declaration to that effect along with his PAN to the person paying or crediting such sum.
 - Taxpoint: Tax is not required to be deducted even if the amount of payment exceeds Rs. 1,00,000/-
 - When tax shall be deducted: At the time of payment or crediting the party, whichever is earlier.
- Rate of TDS
- Individual or HUF 1%
 - Other Payee 2%

TDS on Insurance Commission [Sec. 194D]

- Who is responsible for deducting tax:
 - Any person responsible for paying to a resident person any income by way of remuneration or reward (i.e. commission etc.) for soliciting or procuring insurance business including business relating to the continuance, renewal or revival of policies of insurance.
- Tax shall not be deducted if the aggregate amounts of remuneration or reward credited or paid during the financial year to the payee do not exceed 15,000.

Unit 14: Introduction to Basic Concepts of Income Tax Law

- When tax shall be deducted: At the time of payment or crediting the party, whichever is earlier

Rate of TDS:

- Domestic Company: 10%
- Other Payee: 5%

TDS on Payment in Respect of Life Insurance Policy [Sec. 194DA]

- Who is responsible for deducting tax:

Any person responsible for paying to a resident any sum under a life insurance policy, including the sum allocated by way of bonus on such policy other than the amount not includible in the total income u/s 10(10D).

- TDS is not required to be deducted on any payment which is exempt u/s 10(10D).
- Tax shall not be deducted if the aggregate amount of payments to the payee during the financial year is less than 1,00,000.
- When tax shall be deducted:
 - At the time of payment
- Rate of TDS:
 - 5% (No surcharge, health and education cess) on the income comprised therein.

TDS on Payment to Non-resident Sportsman or Sports Associations [Sec. 194E]

Who is responsible for deducting tax: Any person who is responsible to pay to the Sportsman (including an athlete) or an entertainer being non-resident foreign citizen the income by way of.

1. Participation in India in any game (excluding card games or gambling) or sport
2. Advertising
3. Contribution of articles relating to any game or sports in any newspaper, magazine or journal.

- Rate of TDS:
 - 20% (+ Surcharge + health and education cess)
- When tax shall be deducted:
 - At the time of payment or crediting the party whichever is earlier

Payments in Respect of Deposits under National Savings Scheme, etc. [Sec. 194EE]

- Who is responsible for deducting tax: Any person [i.e. post office] responsible for paying an amount (either principal or interest) referred to in sec. 80CCA(2)(a) [i.e. National Saving Scheme, 1987]
- Note: Tax shall not be deducted at source if the aggregate amount of such payments to the payee during the financial year is less than 2,500. When tax shall be deducted: At the time of payment.
- Rate of TDS:
 - Resident: 10%
 - Non-Resident: 10% (+ Surcharge + Health and Education cess)

TDS on Repurchase of Units of Mutual Fund or Unit Trust of India [Sec. 194F]

- Who is responsible for deducting tax:
 - The person responsible for paying to any person any amount referred to in section 80CCB(2) [i.e. mutual fund or UTI]
- When tax shall be deducted:

At the time of payment Rate of TDS: 20% TDS on Commission on Sale of Lottery Tickets [Sec. 194G]

- Who is responsible for deducting tax:

Any person responsible for paying any income by way of commission, remuneration, or prize (by whatever name called) on lottery tickets to any person, who is stocking, distributing, purchasing, or selling such tickets.

TDS on Rent [Sec. 194-I]

Who is responsible for deducting tax:

Following persons are responsible to deduct tax at source on rent to a resident person –

- Any person, other than individual or HUF; &
- Individual or HUF whose total sales, gross receipts or turnover from business or profession carried on by him exceeds 1 crore in case of business or 50 lakh in case of profession during the financial year immediately preceding the financial year in which such sum is credited or paid
- Note:
 - Tax shall not be deducted if the aggregate amounts of rent credited or paid during the financial year to the payee do not exceed 2,40,000. Taxpoint: Where the share of each co-owner is known, the limit of 2,40,000 is applicable to each co-owner separately.

TDS on Transfer of Certain Immovable Property other than Agricultural Land [Sec. 194-IA]

- When tax shall be deducted: At the time of payment or crediting the payee, whichever is earlier.
- Rate of TDS: 1%

TDS on Payment of Rent by certain individual / HUF [Sec. 194-IB] Amended

- Rate of TDS: 5%
- When TDS cannot be made:
- Where rent for a month or part thereof does not exceed 50,000
- Other Points:
 - The deductor is not required to obtain Tax Deduction Account Number as required u/s 203A.
 - As per provision of sec. 206AA or sec. 206AB, if the payee fails to provide his PAN, TDS is required to be deducted @ 20%.
 - However, deduction under this section shall not exceed the amount of rent payable for the last month of the previous year (or the last month of the tenancy).

TDS on Payment of Certain Sums by E-commerce Operator to E-commerce Participant [194-O]

- When tax shall be deducted: At the time of payment or crediting the payee, whichever is earlier.
- Rate of TDS: 1% of the gross amount of such sales or services or both [if e-commerce participant does not intimate his PAN to eCommerce operator, then rate of TDS is 5%]

14.4 Filing of Return

Different forms of returns of income are prescribed for filing of returns for different Status and Nature of income.

These forms can be downloaded from <https://www.incometax.gov.in/iec/foportal>

Unit 14: Introduction to Basic Concepts of Income Tax Law

- As per provisions of Sec. 139(1), the following persons need to file a return of income in the prescribed form and within the prescribed time –
- A company or a firm Irrespective of the size of income (even where there is a loss): 139(1)(a)
- Any University / College / other institution referred to on Sec. 35(1)(ii) or (iii) Irrespective of the size of income (even where there is a loss): 139(4D) Business Trust Irrespective of the size of income (even where there is a loss): 139(4E)
- Investment Fund referred to in sec. 115UB: 139(4F)
- Any other person where income before giving effect to sec. 54, 54B, 54D, 54EC, 54F, 54G, 54GA, 54GB, and chapter VIA (i.e., deduction u/s 80C to 80U) exceeds the maximum amount which is not chargeable to income tax: 139(1)(b)

Forms - Return Of Income

ITR - 1 (Sahaj)

- For Individuals having Income from Salaries, one house property (does not have any brought forward loss), other sources [Interest (does not have any loss under the head) etc. but except winnings from lottery or income from race horses] and having total income up to 50 lakh

ITR - 2

- For Individuals and HUFs not carrying out business or profession under any proprietorship

ITR - 3

- For individuals and HUFs having income from a proprietary business or profession

ITR - 4 (Sugam)

- For presumptive income from Business & Profession (44AD or 44AE or 44ADA)

ITR - 6

- For Companies other than companies claiming exemption u/s 11

ITR - 7

- For persons including companies required to furnish return u/s 139(4A) or 139(4B) or 139(4C) or 139(4D) or 139(4F)

Belated Return [Sec. 139(4)] Amended

- If an assessee fails to file a return within the time limit allowed u/s 139(1) or within the time allowed under a notice issued u/s 142(1), he can file a belated return.

Time limit:

Assessee may file a such return –

- before 31st December of the relevant assessment year; or before the completion of assessment (u/s 144), - whichever is earlier.
- However, if an assessee files a belated return, he would be liable to fee u/s 234F and interest u/s 234A.

Revised Return [Sec. 139(5)] Amended

- If an assessee discovers any omission or wrong statement (bonafide in nature) in return filed, he can revise his return u/s 139(5).
- Time limit: Assessee may file the revised return –
 - before 31st December of the relevant assessment year; or
 - before completion of regular assessment, whichever is earlier.

- A return of income is said to be defective where all the following conditions are not fulfilled:
 - The return is furnished without paying self-assessment tax along with interest if any.
 - The annexure, statements and columns in the return of income have been duly filled in.

Summary

TDS and TCS are two of the government's most important revenue sources. Additionally, timely tax payments are essential for businesses to make in order to avoid fines and maintain compliance. According to the Income Tax Act, the government predetermines the TDS rates. A tax known as Tax Collected at Source, or TCS, is levied on goods by the seller and is paid by the purchaser at the time of purchase. The goods and services that are covered by TCS are listed in Section 206C of the Income Tax Act of 1961. Income Tax Returns, often known as ITRs, are forms that are used to record gross taxable income, claim tax deductions, and declare net tax liabilities. Individuals who make a particular amount of money are required to file IT returns. Hindu Undivided Families (HUFs), businesses, and self-employed or salaried people all need to file ITRs with the Indian Income Tax Department. The process through which a taxpayer must record all of his income generated within a fiscal year is known as ITR filing. Individuals can complete their return filing through the official portal of the Income Tax Department. ITR 1, ITR 2, ITR 3, ITR 4, ITR 5, ITR 6, and ITR 7 are the seven different forms that it has notified with.

Keywords

Permanent Account Number (PAN): The Income Tax Department will provide any "person" who applies for a Permanent Account Number (PAN), or to whom the department assigns the number without an application, a ten-digit alphanumeric number in the form of a laminated card.

Income Tax Return: The Income-tax Department receives information on a person's income received during a financial year and the taxes that person paid on that income through this prescribed form.

TDS: A mechanism of tax deduction at the moment of income creation is included in the Income-tax Law for speedy and effective tax collection. TDS, or "Tax Deducted at Source," is the name of this system. In accordance with this approach, tax is subtracted from income at the source. On behalf of the payee, the payer withholds tax and remits it to the government.

Self Assessment

1. What is TDS rate (%) under Sec. 192 - Payment of salary if total income exceeds Rs. 50 lakhs but doesn't exceed Rs. 1 crore)?
 - A. 10
 - B. 15
 - C. 20
 - D. 25

2. What is TDS rate (%) under Sec. 192A - Payment of taxable accumulated balance of provident fund?
 - A. 10
 - B. 15
 - C. 20
 - D. 25

3. What is TDS rate (%) under Sec. 194 - Dividend?
 - A. 10

Unit 14: Introduction to Basic Concepts of Income Tax Law

- B. 15
C. 20
D. 25
4. What is TDS rate (%) under Sec. 194B - Winnings from lottery or crossword puzzle or card game or other game of any sort?
A. 10
B. 15
C. 20
D. 30
5. What is TDS rate(%) under Sec. 194BB - Winnings from horse races?
A. 10
B. 15
C. 20
D. 30
6. What is TDS rate(%) under Sec. 194DA - Payment in respect of life insurance policy?
A. 1
B. 15
C. 20
D. 30
7. What is TDS rate(%) under Sec. 194F - Payment on account of repurchase of units of MF or UTI?
A. 1
B. 15
C. 20
D. 30
8. What is TDS rate(%) under Sec. 194G - Commission on sale of lottery tickets?
A. 1
B. 5
C. 20
D. 30
9. What is TDS rate (%) under rent of plant and machinery?
A. 1
B. 2
C. 20
D. 30
10. What is TDS rate (%) under rent of land or building or furniture or fitting
A. 10
B. 20
C. 25
D. 30

11. What is TDS rate (%) under Sec. 194-IA - Payment/credit of consideration to a resident transferor for transfer of any immovable property (other than rural agricultural land)?
 - A. 1
 - B. 2
 - C. 25
 - D. 30

12. What is TDS rate (%) under Section 194S – Payment on transfer of Virtual Digital Asset?
 - A. 1
 - B. 2
 - C. 25
 - D. 30

13. What is TDS rate(%) under Sec. 194D - Insurance commission if recipient is a resident (other than a company)?
 - A. 1
 - B. 5
 - C. 25
 - D. 30

14. What is TDS rate(%) under Sec. 194D - Insurance commission if if recipient is a domestic company?
 - A. 2
 - B. 10
 - C. 25
 - D. 30

15. What is TDS rate (%) under Sec. 194C - Payment or credit to a resident contractor/sub-contractor (payment/credit to an individual or a Hindu undivided family)?
 - A. 1
 - B. 5
 - C. 25
 - D. 30

Answers for Self Assessment

- | | | | | |
|-------|-------|-------|-------|-------|
| 1. A | 2. A | 3. A | 4. D | 5. D |
| 6. A | 7. C | 8. B | 9. B | 10. A |
| 11. B | 12. A | 13. B | 14. B | 15. A |

Review Questions

1. Write a note on Tax deducted at source?
2. What are the rates of TDS for different payments?
3. Explain online filing of returns.

4. What is the utility of PAN?
5. What is the importance of form 26AS?



Further Readings

- https://www.icsi.edu/media/webmodules/16112021_Advance_Tax_Laws.pdf
- Income Tax Law & Practice A.Y 2021-22 by Dr H.C. Mehrotra and Dr. S. P. Goyal. Sahitya Bhawan Publications
- Study Material on Direct Tax Laws and International Taxation by ICAI
- Direct Tax Laws and Practice by Dr. Girish Ahuja & Dr. Ravi Gupta
- <https://incometaxindia.gov.in/Pages/tax-services/file-income-tax-return.aspx>

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