



APPLIED DIRECT TAXATION

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INTERMEDIATE APPLIED DIRECT TAXATION



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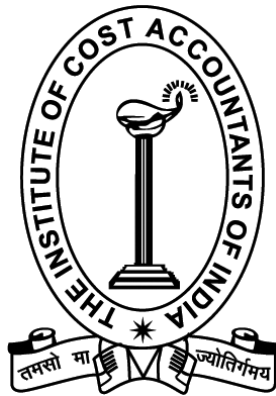
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APPLIED DIRECT TAXATION

**INTERMEDIATE
GROUP - I**

PAPER - 7

STUDY NOTES



**THE INSTITUTE OF
COST ACCOUNTANTS OF INDIA**

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SYLLABUS

OBJECTIVES

To gain knowledge about the tax laws in force for the relevant accounting year and to provide an insight into procedural aspects for filing tax returns for various assesses.

Learning Aims

The syllabus aim to test the student's ability to :

- Explain the basic principles underlying the Income tax Act and Wealth tax Act,
- Compute the income of an individual and business under various heads of income
- Understand Procedure for tax return preparation, filing, assessment and tax refund for various assesses.
- Understand the powers of various assessing authorities.
- Understand appellate procedure under various provisions of these Acts

Skill set required

Level B: Requiring the skill levels of knowledge, comprehension, application, and analysis

1. Direct Taxes- Comprehensive Study. (50%)

- Overview of Direct Tax Laws
- Direct versus indirect taxes, taxable person
- Basic Concepts.
- A comprehensive study of the Income-tax Act, 1961; case laws governing capital and revenue expenditure, deemed income, residence concept.
- Special problems centering on the concept of assessee, registered firm, Hindu Undivided Association of persons and trust, minors, cooperatives, non-resident Indians and avoidance of double taxation.
- Salaries, perquisites, gratuity and retirement benefits, income from house property, capital gains, income from other sources, income from business and profession, problems arising from aggregation of income and set off and carry forward of losses,
- Computation of income and Return of Income Tax, Filing procedure, Principles of valuation of movable and immovable property. Advance payment of Tax.
- Deduction and collection of tax at source.
- Tax incentives and export promotion schemes, other benefits and tax exemptions.
- Assessment, appeals, revisions, review, rectification and application to Central Board of Direct Taxes.
- Penalties, Fines and prosecution.
- Refunds.
- Securities Transaction Tax.
- Fringe Benefit Tax.
- Banking Cash Transaction Tax.
- Wealth Tax.

2. Practical problems and case studies under Direct Taxes. (50%)

Paper 7
APPLIED DIRECT TAXATION

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STUDY NOTE - 1

TYPES OF TAXES

This Study Note includes

- Basis For Taxation
- Direct Taxes and Indirect Taxes

1.1 BASIS FOR TAXATION

India is a socialist, democratic and republic state. Constitution of India is supreme law of land. All other laws, including the Income-tax Act, are subordinate to the Constitution of India. The Constitution provides that 'no tax shall be levied or collected except by authority of law'. The Constitution includes three lists in the Seventh Schedule providing authority to the Central Government and the state governments to levy and collect taxes on subjects stated in the lists.

Powers of Central or State Government to levy tax

Article	Empowers	For
246(1)	Central or State Government	Levy of various taxes.
246(1)	Central Government	Levy taxes in List I of the Seventh Schedule of the constitution.
246(3)	State Government	Levy taxes in List II of the Seventh Schedule of the Constitution.
—	Central and State Government	List III of Seventh Schedule.

List I: Union List

- Entry No. 82 : Income Tax other than Tax on Agricultural Income
- Entry No. 83 : Customs duties including export duties
- Entry No. 84 : Union Excise Duty (other than liquor, opium, etc.)
- Entry No. 85 : Corporation Tax
- Entry No. 92A : Taxes on Inter-State Sales (CST)
- Entry No. 92B : Tax on Inter-State Consignment of Goods (not yet considered by GOI)
- Entry No. 92C : Taxes on services
- Entry No. 97 : Any other matter not included in List II or List III
[Levy of Service Tax through Finance Act, 1994]

List II: State List

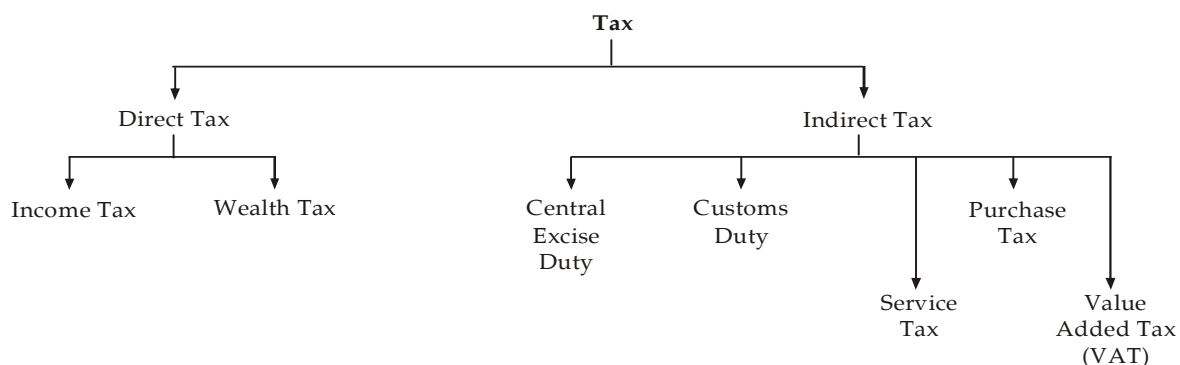
- Entry No. 46 : Agricultural Income Tax
- Entry No. 51 : State Excise Duty
- Entry No. 52 : Tax on Entry of Goods into local area for consumption or use or sale (called octroi)
- Entry No. 54 : Tax on intra State Sales (Local/General Sales Tax)

List III : State List

Entry No. 17A : Forests

Entry No. 25 : Education

1.2 DIRECT TAXES AND INDIRECT TAXES



Basis of difference between Indirect Tax and Direct Tax

Basis of difference	Indirect Tax	Direct Tax
1. Taxable Event	Purchase / Sale / Manufacture of goods and provision of services	Taxable Income / Taxable Wealth of the Assessee.
2. Levy & Collection	Levied & collected from the consumer but paid / deposited to the Exchequer by the Assessee / Dealer	Levied and collected from the Assessee
3. Shifting of Burden	Tax burden is shifted to the subsequent / ultimate user	Directly borne by the Assessee. Hence, cannot be shifted.
4. Collected	At the time of sale of purchases or rendering of services	after the income for a year is earned or valuation of assets is determined on the valuation date.

STUDY NOTE - 2

THE SOURCE OF INCOME TAX LAW

This Study Note includes

- Basic Concepts
- Rates of Income Tax for A.Y. 2012-13
- Definition
- Heads of Income

2.1 BASIC CONCEPTS

THE ELEMENTS / SOURCES OF INCOME TAX LAW

1. The Income Tax Act, 1961

- (a) Income tax in India is governed by the Income Tax Act, 1961
- (b) It came into force w.e.f. 1.4.1962
- (c) The Act contains 298 sections and XIV Schedules
- (d) The Finance Act shall bring amendment to this Act.
- (e) The Law provides for determination of taxable income, tax liability and procedure for assessment, appeal, penalties and prosecutions.

2. Finance Act

- (a) Finance Minister presents this as Finance Bill in both the Houses of Parliament.
- (b) Part A of the Budget contains proposed policies of the Government in fiscal areas.
- (c) Part B contains the detailed tax proposals.
- (d) Once the Finance Bill is approved by the Parliament and gets the assent of the President, it becomes the Finance Act.
- (e) The rate of tax at which income shall be charged is prescribed in the Schedule I of Finance Act.
- (f) The Finance Act brings amendments to both the Direct Tax Laws (i.e. Income Tax, Wealth Tax etc.) and Indirect Tax Laws (i.e. law relating to Central Excise, Customs Duty, Service Tax etc.)

3. The Income Tax Rules, 1962

- (a) The administration of Direct Taxes is vested with Central Board of Direct Taxes (CBDT).
- (b) Under Section 295 of IT Act, CBDT is empowered to frame rules from time to time to carry out the purpose and proper administration of the Act.
- (c) All forms, procedures and principles of valuation of perquisites prescribed under the Act are provided in the Rules framed by CBDT.

4. Circulars / Notifications from CBDT

- (a) In exercise of the powers u/s 119, CBDT issues circulars and notifications from time to time.
- (b) These circulars clarify doubts regarding the scope and meaning of the various provisions of the Act.
- (c) These circulars act as guidance for officers and assesses.
- (d) These circulars are binding on Assessing Officers but not on assesses and Courts.
- (e) The circulars issued by the CBDT shall not be in contrary to the provisions of the Act.



Subordinate Legislation

The Government enacts the law in the Parliament, there e.g. Income Tax Act, Central Excise Act, etc. where is a need for detailed rules and regulations, the enactment is to be done by either CBDT or CBEC. The rules and regulations enacted by CBDT or CBEC i.e. Income Tax Rules, Cenvat Credit Rules, the Notifications and Circulars issued by CBDT, CBEC is called Subordinate Legislation.

5. Supreme Court and High Court Decisions

- The Supreme Court and the High Court can give judgment **only on the question of law.**
- The Law laid down by the Supreme Court is the law of the land.
- The decision of High Court will apply in the respective States, within its jurisdiction.

DETERMINING THE RATES OF TAX UNDER THE INCOME TAX ACT, 1961

- Income Tax shall be charged at the rates fixed for the year by the Annual Finance Act.
- The First Schedule to the Finance Act provides the following rates of taxation.

Part I	The tax rates applicable to income of various types of assessee for the assessment year
Part II	Rates of TDS for the current Financial year
Part III	Rates of TDS for salary and advance tax (which becomes Part I of the next assessment year)

2.2 RATES OF INCOME-TAX FOR ASSESSMENT YEAR 2012-13

Normal Rates of Income Tax

I. In the case of every Individual or Hindu undivided family or AOP/BOI (other than a co-operative society) whether incorporated or not, or every artificial judicial person

Upto ₹ 1,80,000	Nil
₹ 1,80,010 to ₹ 5,00,000	10%
₹ 5,00,010 to ₹ 8,00,000	20%
Above ₹ 8,00,000	30%

II. In the case of every **individual**, being a **woman resident in India**, and **below the age of sixty years** at any time during the previous year.

Upto ₹ 1,90,000	Nil
₹ 1,90,010 to ₹ 5,00,000	10%
₹ 5,00,010 to ₹ 8,00,000	20%
Above ₹ 8,00,000	30%

III. In the case of every **individual**, being a **resident in India**, who is of the **age of 60 years or more** at any time during the previous year. [*Senior citizen*]

Upto ₹ 2,50,000	Nil
₹ 2,50,010 to ₹ 5,00,000	10%
₹ 5,00,010 to ₹ 8,00,000	20%
Above ₹ 8,00,000	30%

IV. In the case of every **individual**, being a **resident in India**, who is of the **age of 80 years or more** at any time during the previous year. [**Very senior citizen**]

Upto ₹ 5,00,000	Nil
₹ 5,00,010 to ₹ 8,00,000	20%
Above ₹ 8,00,000	30%

Note : No surcharge is payable by the above assessees.

'Education Cess' @ 2%, and 'Secondary and Higher Education Cess (SHEC)' @ 1% on income tax shall be chargeable.

2.2.2 Other Assesseees :

Assessee	Rate of Tax	Surcharge
For Firms (including limited liability partnership)	Total Income × 30% + EC @ 2% + SHEC @ 1%.	Surcharge — NIL
Domestic Companies	Total Income × 30% + EC @ 2% + SHEC @ 1%.	Surcharge @ 5% if the total income exceeds ₹ 1 crore
Foreign Companies Other Income Royalty received from Indian Government or an Indian concern in pursuance of an agreement made by it with the Indian concern after March 31, 1961, but before April 1, 1976, or fees for rendering technical services in pursuance of an agreement made by it after February 29, 1964 and where such agreement has, in either case been approved by the Central Government	Total Income × 40% + EC @ 2% + SHEC @ 1%	Surcharge @ 2% if the total income exceeds ₹ 1 crore
For Local Authorities	Total Income × 30% + EC @ 2% + SHEC @ 1%.	(Surcharge is not applicable) Nil
For Co-operative Societies	For First ₹ 10,000 @ 10% For Next ₹ 10,000 @ 20% For the Balance @ 30% EC @ 2% and SHEC @ 1% are applicable.	Surcharge is not applicable. Nil
MAT = Minimum Alternate Tax	18.5% of Book Profit + EC 2% + SHEC 1%	Surcharge if Book Profits exceed ₹ 1 crore.

2.3 DEFINITION

Assessee means: [Section 2(7)]

Any person who is liable to pay any tax or any other sum under the Income Tax Act, 1961, and

Assessee includes

- Every person in respect of whom any proceedings has been taken for the assessment of
 - **His income or Fringe Benefits** or of the income of any other person.
 - **Loss** sustained by him or other person.
 - **Refund** due to him or such other person.
- Every person who is **deemed to be an assessee** under the Act.
- Every person who is **deemed to be an assessee in default** under the Act.



Assessment Year [Section 2 (9)]

1. Assessment Year means the **period of twelve months commencing on the 1st day of April every year.**
2. The year for which tax is paid is called Assessment Year.

The present Assessment Year is 2012-13 relating to previous year 2010-11.

Previous Year [Section 3]

1. Previous Year means **Financial Year** immediately preceding the Assessment Year.
2. The year in respect of the income of which tax is levied is called Previous Year.

The present previous year 2011-12 and its Assessment Year is 2012-13.

Note: Previous Year for Newly established business From the date of setting up of the business to the end of the Financial year in which business was set up.

Example : X Ltd. Started business on 1.11.11. So for X Ltd. Previous year will be considered as 1.11.11 to 31.3.12.

Income [Section 2(24)] includes:

1. Profits or gains of business or profession.
2. Dividend.
3. Voluntary Contribution received by a Charitable / Religious Trust or University / Education Institution or Hospital
4. Value of perquisite or profit in lieu of salary taxable u/s 17 and special allowance or benefit specifically granted either to meet personal expenses or for performance of duties of an office or an employment of profit.
5. Export incentives, like Duty Drawback, Cash Compensatory Support, Sale of licences etc.
6. Interest, salary, bonus, commission or remuneration earned by a partner of a Firm from such Firm.
7. Capital Gains chargeable u/s 45.
8. Profits and gains from the business of banking carried on by a cooperative society with its members.
9. 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.
10. Deemed income u/s 41 or 59.
11. Sums received by an assessee from his employees towards welfare fund contributions such as Provident Fund, Superannuation Fund etc.
12. Amount received under Keyman Insurance Policy including bonus thereon.
13. Amount received under agreement for (a) not carrying out activity in relation to any business, or (b) not sharing any knowhow, patent, copyright etc.
14. Benefit or perquisite received from a Company, by a Director or a person holding substantial interest or a relative of the Director or such person.
15. Gift as defined u/s 56 (2)(vi) (w.e.f. A.Y 2008-2009). Any sum of money exceeding ₹ 50,000, received by an Individual or a HUF from any person during the previous year without consideration on or after 1.4.2007, then the whole of aggregate of such sums will be taxable.

PREVIOUS YEAR & ASSESSMENT YEAR WILL BE SAME in the following cases:

1. Shipping business of nonresident [Section 172]
2. Persons leaving India [Section 174]
3. AOP or BOI or Artificial Juridical Person formed for a particular event or purpose [Sec. 174A]
4. Persons likely to transfer property to avoid tax [Section 175]
5. Discontinued business [Section 176]

UNDISCLOSED SOURCES OF INCOME

1. Unexplained Cash Credits u/s 68
2. Unexplained investments u/s 69
3. Unexplained money, bullion or jewel or valuable article u/s 69A



4. Undisclosed investments u/s 69B
5. Unexplained expenditure u/s 69C
6. Amount borrowed or repaid on hundi, other than by way of account payee cheque u/s 69D.

Application of Income

An obligation to apply income, which has accrued or has arisen or has been received amounts to merely the apportionment of income. Therefore the essentials of the concept of application of income under the provisions of the Income Tax Act are :

1. Income accrues to the assessee
2. Income reaches the assessee
3. Income is applied to discharge an obligation, whether self-imposed or gratuitous.

Diversion of Income

An obligation to apply the income in a particular way before it is received by the assessee or before it has arisen or accrued to the assessee results in diversion of income. The source is charged with an overriding title, which diverts the income. Therefore the essentials are the following :

1. Income is diverted at source,
2. There is an overriding charge or title for such diversion, and
3. The charge / obligation is on the source of income and not on thereceiver.

Examples of diversion by overriding title are -

- (a) Right of maintenance of dependants or of coparceners on partition
- (b) Right under a statutory provision
- (c) A charge created by a decree of a Court of law.

TOTAL INCOME [Sec. 2(45)]

“Total income” means the total amount of income as referred to in sec. 5 and computed in the manner laid down in the Act. Total income constitutes the tax with reference to which income tax is charged.

GROSS TOTAL INCOME [Section 80B]

Gross Total Income means total income computed in accordance with the provisions of the Income Tax Act before making any deduction under Chapter VIA.

ROUNDING OFF TOTAL INCOME AND TAX

Rounding Off Income [Section 288A] : The Total Income computed under this Act, shall be rounded off to the nearest multiple of ₹ 10.

Rounding Off Tax [Section 288B] : The amount of Tax including Tax Deducted at Source (TDS) and advance tax, interest, penalty, fine or any other sum payable, and the amount of refund due under the Income Tax Act, shall be rounded off to the **nearest Ten Rupees**.

BOOKS OF ACCOUNT [Sec. 2(12A)]

It includes ledgers, day books, cash books, account-books and other books, whether kept in the written form or as printouts or data stored in a floppy, disc, tape or any other form of electromagnetic data storage device.

DOCUMENT [Sec. 2(22AA)]

It includes an electronic record as defined in clause (t) of sub-section (1) of section 2 of the Information Technology Act, 2000 (21 of 2000).

**RELATIVE [Sec. 2(41)]**

In relation to an individual, means the husband, wife, brother or sister or any lineal ascendant or descendant of that individual.

RESULTING COMPANY [Sec. 2(41A)]

It means one or more companies (including a wholly owned subsidiary thereof) to which the undertaking of the demerged company is transferred in a demerger and, the resulting company in consideration of such transfer of undertaking, issues shares to the shareholders of the demerged company and includes any authority or body or local authority or public sector company or a company established, constituted or formed as a result of demerger.

INSURER [Sec. 2(28BB)]

It means an insurer being an Indian insurance company, as defined under clause (7A) of section 2 of the Insurance Act, 1938 (4 of 1938), which has been granted a certificate of registration under section 3 of that Act.

SUBSTANTIAL INTEREST [Sec. 2 (32)]

Person who has a substantial interest in the company, in relation to a company, means a person who is the beneficial owner of shares, not being shares entitled to a fixed rate of dividend whether with or without a right to participate in profits, carrying not less than twenty per cent of the voting power. In the case of a non-corporate entity, a person can be said to have substantial interest if 20% or more share of profit is held.

INFRASTRUCTURAL CAPITAL COMPANY [Sec.2(26A)]

"Infrastructure capital company" means such company which makes investments by way of acquiring shares or providing long-term finance to any enterprise or undertaking wholly engaged in the business referred to in sub-section (4) of section 80 -IA or sub-section (1) of section 80-IAB or an undertaking developing and building a housing project referred to in sub-section (10) of section 80- IB or a project for constructing a hospital with at least one hundred beds for patients.[Sec. 2(26A)].

INFRASTRUCTURAL CAPITAL FUND [Sec.2(26B)]

"Infrastructure capital fund" means such fund operating under a trust deed registered under the provisions of the Registration Act, 1908 established to raise monies by the trustees for investment by way of acquiring shares or providing long-term finance to any enterprise or undertaking wholly engaged in the business referred to in sub-section (4) of section 80-IA or sub-section (1) of section 80- IAB or an undertaking developing and building a housing project referred to in sub-section (10) of section 80-IB or a project for constructing a hotel of not less than three star category as classified by the Central Government or a project for constructing a hospital with at least one hundred beds for patients. [Sec 2(26B)].

CHARGE OF INCOME TAX [Sec. 4]

According to sec. 4 of the Income-tax, 1961 the following basic principles are followed while charging income-tax—

- (i) income-tax is a tax on the annual income of an assessee,
- (ii) usually, the income of the Previous Year (PY) is charged to the following Assessment Year (AY) at the prescribed rate fixed by the relevant Financial Act, and
- (iii) tax is levied on the total income of every assessee

RECEIPT OF INCOME - DEEMED INCOME [Sec. 7]

The following income shall be deemed to be received in the Previous Year :

- (i) Employers contribution to recognized provident fund in excess of 12% of salary and interest credited to the recognized provident fund in excess of 9.5%

- (ii) The transfer balance in a recognized provident fund, to the extent provided in sub rule (4) of rule 11 of part A of fourth schedule.

DIVIDEND INCOME [Sec. 8]

Dividend include—

- (a) any distribution by a company of accumulated profits whether capitalised or not, if such distribution entails the release by the company to its shareholders of all or any part of the assets of the company ;
- (b) any distribution to its shareholders by a company of debentures, debenture-stock, or deposit certificates in any form, whether with or without interest, and any distribution to its preference shareholders of shares by way of bonus, to the extent to which the company possesses accumulated profits, whether capitalised or not ;
- (c) any distribution made to the shareholders of a company on its liquidation, to the extent to which the distribution is attributable to the accumulated profits of the company immediately before its liquidation, whether capitalised or not ;
- (d) any distribution to its shareholders by a company on the reduction of its capital, to the extent to which the company possesses accumulated profits⁸⁵ which arose after the end of the previous year ending next before the 1st day of April, 1933, whether such accumulated profits have been capitalised or not ;
- (e) any payment by a company, not being a company in which the public are substantially interested, of any sum (whether as representing a part of the assets of the company or otherwise) [made after the 31st day of May, 1987, by way of advance or loan to a shareholder being a person who is the beneficial owner of shares (not being shares entitled to a fixed rate of dividend whether with or without a right to participate in profits) holding not less than ten per cent of the voting power, or to any concern in which such shareholder is a member or a partner and in which he has a substantial interest (hereafter in this clause referred to as the said concern)] or any payment by any such company on behalf, or for the individual benefit, of any such shareholder, to the extent to which the company in either case possesses accumulated profits;

But “dividend” does not include—

- (i) a distribution made in accordance with sub-clause (c) or sub-clause (d) in respect of any share issued for full cash consideration, where the holder of the share is not entitled in the event of liquidation to participate in the surplus assets ;
- (ia) a distribution made in accordance with sub-clause (c) or sub-clause (d) in so far as such distribution is attributable to the capitalised profits of the company representing bonus shares allotted to its equity shareholders after the 31st day of March, 1964,
- (ii) any advance or loan made to a shareholder [or the said concern] by a company in the ordinary course of its business, where the lending of money is a substantial part of the business of the company ;
- (iii) any dividend paid by a company which is set off by the company against the whole or any part of any sum previously paid by it and treated as a dividend within the meaning of sub-clause (e), to the extent to which it is so set off;
- (iv) any payment made by a company on purchase of its own shares from a shareholder in accordance with the provisions of section 77A of the Companies Act, 1956 (1 of 1956);
- (v) any distribution of shares pursuant to a demerger by the resulting company to the shareholders of the demerged company (whether or not there is a reduction of capital in the demerged company)

Explanation 1.—The expression “accumulated profits”, wherever it occurs in this clause, shall not include capital gains arising before the 1st day of April, 1946, or after the 31st day of March, 1948, and before the 1st day of April, 1956.



Explanation 2.—The expression “accumulated profits” in sub-clauses (a), (b), (d) and (e), shall include all profits of the company up to the date of distribution or payment referred to in those sub-clauses, and in sub-clause (c) shall include all profits of the company up to the date of liquidation, [but shall not, where the liquidation is consequent on the compulsory acquisition of its undertaking by the Government or a corporation owned or controlled by the Government under any law for the time being in force, include any profits of the company prior to three successive previous years immediately preceding the previous year in which such acquisition took place].

Explanation 3.—For the purposes of this clause,—

- (a) “concern” means a Hindu undivided family, or a firm or an association of persons or a body of individuals or a company ;
- (b) a person shall be deemed to have a substantial interest in a concern, other than a company, if he is, at any time during the previous year, beneficially entitled to not less than twenty per cent of the income of such concern;

CAPITAL AND REVENUE RECEIPTS

The objective of the Income-tax Act is to tax only income generally revenue receipts unless specifically exempted. On the other hand capital receipts are not chargeable to tax except when specifically provided in the Act. The distinction between a capital receipt and a revenue receipt should be perceived based on the facts and circumstances of each case. There is no specific provision in the Act to distinguish between a capital receipt and revenue receipt. It may be observed that :

A receipt in substitution of a source of income is a capital receipt while a receipt in substitution of an income is a revenue receipt.

An amount received as a compensation for surrender of certain rights under an agreement is a capital receipt whereas an amount received under an agreement as compensation for loss of future profit is a revenue receipt.

CAPITAL AND REVENUE EXPENDITURE

In computing taxable income normally revenue expenditure incurred for the purpose of earning income is deductible from revenue receipt unless the law provides specific rules to disallow such expenditure wholly or partly. On the other hand capital expenditure is not deductible while computing taxable income unless the law expressly so provides.

Neither the capital expenditure nor revenue expenditure has been defined in the Act. However, from the facts and circumstances of each case and from the judicial decisions the following general principles to be kept in mind :

- (i) Capital expenditure is incurred in acquiring, extending or improving a fixed asset whereas revenue expenditure is incurred in the normal course of business as a routine expenditure.
- (ii) Capital expenditure incurred for enduring benefits whereas revenue expenditure is consumed within a Previous Year .
- (iii) Capital expenditure makes improvement with earning capacity of a business whereas a revenue expenditure maintains the profit making capacity of a business.
- (iv) Capital expenditure is a nonrecurring expenditure whereas revenue expenditure is normally a recurring one.

2.4 “HEADS OF INCOME” [Sec 14]

Significance of Heads of Income :

1. The income chargeable under a particular head **cannot be charged under any other head**.
2. The Act has **self contained** provisions in respect of each head of income.
3. If any income is **charged under a wrong head** of income, the assessee will **lose the benefit** of deduction available to him under that head.

Relevance of method of accounting for heads of income :

Heads of Income	Relevance of Method of Accounting
Chapter IV-A Salaries (15 - 17)	1. Taxable on due basis or on receipt basis , whichever is earlier. 2. Method of accounting is irrelevant .
Chapter IV-C House Property (22 - 27)	1. Income from house property is taxable only on accrual basis . 2. Method of accounting is not relevant .
Chapter IV-D Business Income (28-44DB)	1. U/s 145 assessee may follow either Cash or Mercantile system of accounting regularly employed by the assessee. 2. Exceptions : Certain payments are allowable only on actual payment basis. Accrual concept does not hold good - (a) Employer's contribution to PF, ESI, Tax, Duty, Cess, Fees to Government, Interest on loans and advances from banks and financial institutions, provision for leave encashment, bonus or commission etc. (b) Telecommunication Licence Fee is allowable in instalments only from the year of payment. (c) Preliminary Expenses distributed over five years. (d) Amalgamation / Demerger Expenses distributed over five years. (e) Amount paid in connection with Voluntary Retirement Scheme distributed over five years.
Chapter IV-E Capital Gains (45 - 55A)	1. Income from capital gains shall be taxable during the previous year Capital Gains in which the Capital Asset is transferred (i.e) year of accrual . 2. The method of accounting is not relevant for taxing the income under the head capital gains.
Chapter IV-F Other Sources (56 - 59)	U/s 145 assessee may follow either on Cash or Mercantile system of accounting regularly employed by the assessee.



STUDY NOTE - 3

RESIDENTIAL STATUS AND TAX INCIDENCE

This Study Note includes

- Introduction
- Residential status of Individuals
- Residential status of Hindu Undivided Family
- Residential status of a Company
- Residential status of Firm and Association of Persons
- Residential status of Every Other Person
- Status and Incidence of Income-Tax

3.1 INTRODUCTION

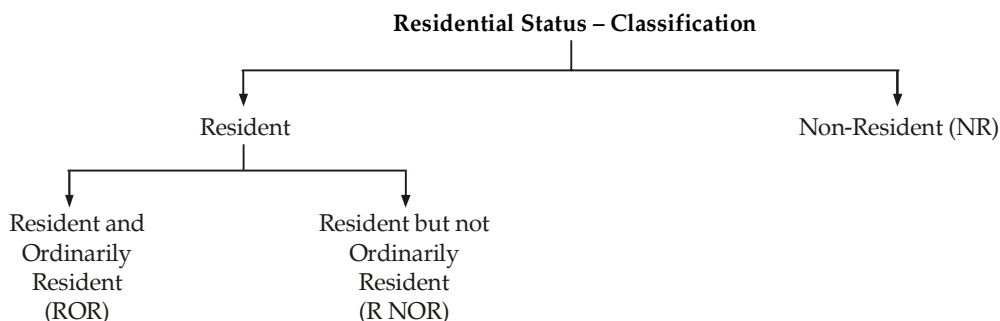
3.1.1 Residential Status

The residential status of a person as referred in Sec. 2(31) of the Act. for each assessment year under consideration to determine the scope of total income.

3.1.2 Importance

- Total income of an assessee cannot be determined without knowing his residential status.
- The residential status shall be determined for every person for each previous year independently.
- The onus of responsibility to prove the residential status is on the assessee.

3.2 RESIDENTIAL STATUS OF INDIVIDUALS [SEC.6(1)]



1. Basic Conditions:

- If the Individual **stayed** in India for a period of **182 DAYS OR MORE** during the **Relevant Previous Year (RPY)** he is **Resident of India (OR)**
- If he stayed in India for a period of **60 DAYS OR MORE** during **Relevant Previous Year (RPY)** and **365 DAYS OR MORE** during the four preceding previous years he is **Resident of India**.

If the above two conditions are not satisfied, he is **NonResident**.

Note: The day on which he enters India as well as the day on which he leaves India shall be taken into account as the stay of the Individual in India.

Special Exceptional Situations:

For the following persons, condition mentioned in 1(a) above only shall apply to determine their Residential Status

- (a) Individual, Indian citizen, leaving India for employment outside India, or
- (b) Indian Citizen being a crew member of an Indian ship leaving India, or
- (c) Individual, Indian citizen or person of Indian origin, visiting India.

Additional Conditions: Sec. 6(6)(a)

- 1. Resident in India for at least 2 years out of the preceding 10 previous years.
- 2. Physically present in India for at least 730 days during the 7 preceding previous years.

Status of an Individual	Basic condition	Additional condition/(s)
Resident and ordinarily Resident u/s 6(6)	Satisfies	Satisfies both the conditions
Resident but not ordinarily Resident u/s 6(6)	Satisfies	May or may not satisfy any of the additional condition
Non Resident	Fails to satisfy	Not required to check

3.3 RESIDENTIAL STATUS OF HUF/FIRM/AOP/EVERY OTHER PERSON [Sec. 6(2), SEC.6(4)]

Control and Management is	Residential Status
1. Wholly or partly in India	Resident
2. Wholly outside India	Non-resident

3.4 RESIDENTIAL STATUS OF A COMPANY [SECTION 6 (3)]

1. Indian Company	Resident
2. Other Companies - Control and management is	
(a) Wholly in India	Resident
(b) Wholly or partly outside India	Non-resident

If a person is a resident for one source of income in a previous year, he shall be deemed to be a resident for all other sources of income also. [Section 6(5)]

3.5 STATUS AND INCIDENCE OF INCOME-TAX

The incidence of tax on a tax-payer depends on his residential status as well as on the place and time of accrual or receipt of income. A suitable table is given below :



Particulars of Income	Tax incidence in case of —		
	Resident	Resident but not ordinarily resident	Non-resident
a. Income received in India whether accrued in India or outside India	Yes	Yes	Yes
b. Income deemed to be received in India whether accrued in India or outside India.	Yes	Yes	Yes
c. Income accruing or arising in India whether received in India or outside India.	Yes	Yes	Yes
d. Income deemed to accrue or arise in India, whether received in India or outside India.	Yes	Yes	Yes
e. Income received and accrued outside India from a business controlled in profession set up in India	Yes	Yes	No
f. Income received and accrued outside India from a business controlled from outside India or profession set up outside India.	Yes	No	No
g. Income earned and received outside India but later on remitted to India.	No	No	No
Total	a to f	a to e	a to d

PROBLEMS ON RESIDENTIAL STATUS AND TAX INCIDENCE

Problem 1. X, after about 30 years' stay in India, returns to America on January 29, 2009. He returns to India in June 2011 to join an American company as its overseas branch manager. Determine his residential status for the assessment year 2012-13.

Solution : For the assessment year 2012-13, the year 2011-12 is the previous year. During 2011-12, X is in India for more than 274 days. He is, therefore, resident in India. He is resident in India for 2 years out of 10 years (i.e., 2001-2002 to 2010-11), and he has stayed for more than 730 days during the seven years preceding the previous year 2011-12. He is, therefore, resident and ordinarily resident in India for the assessment year 2012-13.

Problem 2. Indian citizen and businessman Shri Hari, who resides in Kolkata, went to France for employment purposes on 15.8.2011 and came back to India on 10.11.2012. He has never been out of India in the past.

(a) Determine residential status of Shri Hari for the assessment year 2012-13.

(b) Will your answer be different if he had gone on a leisure trip?

Solution :

- (a) The previous year for the assessment year 2012-13 is 2011-12. During this period he was in India for 137 days (30+31+30+31+15). As he is not in India for 182 days, he does not satisfy the first condition of category A. The second condition of category 'A' is also not satisfied because he is a citizen of India and leaves India during the previous year for employment outside India and is therefore, covered under exception No. 1 where 60 days will be substituted by 182 days.

- (b) In this case, although he does not satisfy the first condition of category A, he satisfies the second condition as he was in India for more than 60 days in the relevant previous year and was also here for more than 365 days during four preceding previous years. He is therefore, resident in India. The exception will not be applicable to him because he did not leave India for the purpose of employment. He satisfies both the conditions of category B because he was always been in India before 15.8.2011.

The status of the assessee for the previous year 2011-12 will in this case be resident and ordinarily resident in India.

Problem 3. 'B', an Indian citizen left India for the first time on 21.9.2010 for employment in Denmark. During the previous year 2010-11 he comes to India on 5.5.2011 for 150 days. Determine the residential status of 'B' for assessment years 2011-12 and 2012-13.

Solution : During the previous year 2010-11 'B' was in India for 174 days (30+31+30+31+31+21) and therefore, does not satisfy the first condition. As regards the second condition, although he was here in the four preceding previous years for more than 365 days as he was permanently in India but for the relevant previous year 2010-11 he should have been here for 182 days instead of 60 days as he is a citizen of India and leaves India in 2010-11 for employment abroad.

He neither satisfies the first, nor the second condition and is therefore, Non-Resident in India.

Similarly, during the previous year 2011-12 he visits India for 150 days. In this case also, the period of 60 days will be substituted by 182 days as he is a citizen of India. Therefore, he will be a Non-Resident in India even for previous year 2011-12.

Problem 4. Subhash discloses following particulars of his receipts during the Previous Year 2011-2012:

(i) Salary income earned at Pune but received in Srilanka	2,50,000
(ii) Profits earned from a business in Kenya which is controlled in India, half of the profits being received in India.	2,20,000
(iii) Income from property, situated in Nairobi and received there	75,000
(iv) Income from agriculture in Bangladesh and brought to India	68,000
(v) Dividend-paid by an Indian company but received in London on 15 May 2011.	22,000
(vi) Interest on USA Development Bonds and one half of which was received in India	44,000
(vii) Past foreign untaxed income brought to India	2,10,000
(viii) Gift of \$1000 from father, settled in USA, received in India	80,000
(ix) Land sold in Delhi, consideration received in Canada, resulting into capital gain	2,50,000
(x) Income from structure-designing consultancy service, set up in Germany, controlled from India, profits being received outside India	4,00,000
(xi) Loss from foreign business, controlled from India, sales being received in India	(-) 2,00,000

Determine his taxable income for the previous year 2011-2012 if he is (i) resident and ordinarily resident, (ii) resident but not ordinarily resident, (iii) non-resident.

Solution :

Particulars of Income	Resident and ordinarily resident ₹	Resident but not ordinarily resident ₹	Non-resident ₹
(i) Salary earned at Pune but received at Sri Lanka: Salary is deemed to accrue or arise at a place where services are rendered, place of receipt being immaterial [Sec. 9(1)(ii)]. Hence, it is taxable in all cases	2,50,000	2,50,000	2,50,000
(ii) Profits earned from a business in Kenya, controlled in India:			
(a) One half of profits are taxable on receipt basis	1,10,000	1,10,000	1,10,000
(b) Other half profits—from foreign business controlled in India (in case of resident and ordinarily resident, place of control is of no relevance)	1,10,000	1,10,000	—
(iii) Income from property in Nairobi and received there: Income accruing or arising outside India	75,000	—	—
(iv) Income from agriculture in Bangladesh and brought to India: It is not income received in India as receipt means first receipt. Hence, it is not taxable in case of “not ordinarily resident” and “non-resident”. In case of “ordinarily resident”, it is income accruing or arising outside India. Hence, it is taxable. It should be noted that it is not agricultural income/as it is not derived from land, situated in India, and hence not derived from under Sec. 10(1).	68,000	—	—
(v) Dividend paid by an Indian company but received in London: Dividend paid by an Indian company is deemed to accrue or arise in India. However, any dividend paid, declared or distributed by a domestic company on or after 1 st April 2005 is exempt from tax under Sec. 10(34). Therefore, such dividend is not taxable.	—	—	—
(vi) Interest on USA Development Bonds:			
(a) One half is taxable on receipt basis	22,000	22,000	22,000
(b) Other half is taxable only in case of “ordinarily resident” as it is foreign income accruing or arising outside India	22,000	—	—
(vii) Past untaxed foreign income brought to India. It is not income received in India. Furthermore, it is not the income of the previous year 2010-2011. Hence, it is not taxable in any case.	—	—	—
(viii) Gift from a relative is not taxable.	—	—	—

(ix) Capital gain is deemed to accrue or arise in India [Sec. 9(1)(i)]	2,50,000	2,50,000	2,50,000
(x) Income from consultancy profession, set up outside India, profits being received outside India: Taxable in case of "ordinarily resident", as income accruing arising outside India and received outside India [Sec. 5(1)(c)] In case of "not-ordinarily resident", as it is not income from profession set up in India, control and management applies to business and not to professions. Hence, it is not taxable [Sec. 5(1) (c) r. w. Proviso]	40,000	—	—
(xi) Loss from foreign business, controlled from India:- Income includes loss also. Profits are imbedded in sales. As sales were received in India, the place of control and management is not relevant. Business loss can be set off against business profits and thereafter against the income of any other head except income from salary and chance winnings (Sec. 70)	(-) 2,00,000	(-) 2,00,000	(-) 2,00,000
Total Income	11,07,000	5,42,000	4,32,000

Problem 5. Mr.Tajuddin, Indian citizen, earns the following incomes during the previous year 2011-2012 :

Particulars	₹
(i) Profits from a business in Mumbai, managed from France	6,20,000
(ii) Pension for services rendered in Kenya but kept with State Bank in Kenya with the permission of the Reserve Bank of India	1,60,000
(iii) Income from property in Kuwait, received in India	1,58,000
(iv) Profits from business in Nepal and deposited in a bank there	12,000
(v) Income received in Oman from a profession, which was set up in India, extended to Oman and managed from Kenya	1,70,000
(vi) Profit on sale of machinery in India but received in Italy	1,26,000
(vii) Profits, before allowing depreciation, from business Kuwait 50% of profits were received in India Total deprecation	2,00,000 2,50,000
(viii) Interest on foreign bank deposit, received by his minor son in India. Bank deposit was made out of funds gifted by grandfather	1,70,000
(ix) A German company credited commission to his bank account outside India for sale of goods by him in India	1,75,000
(x) Commission earned and received by him outside India on export orders collected by him in India for foreign exporters, without any authority being given to him by them	2,30,000
(xi) Dividends remitted in India by an Egyptian company to him under his instruction through Bank of Patiala	1,80,000

Determine his taxable income for the previous year 2011-2012 if he is (i) resident and ordinarily resident; (ii) resident but not ordinarily resident; and (iii) non-resident

Solution :

Particulars of Income	Resident and ordinarily resident ₹	Resident but not ordinarily resident ₹	Non-resident
(i) Profits from a business at Mumbai, managed from France : Income from business accrues at the place where business is done, place of management being of no relevance. Hence, it is taxable in all cases	6,20,000	6,20,000	6,20,000
(ii) Pension for services rendered in Kenya, received there: Pension is deemed to accrue or arise at a place where services were rendered	1,60,000	—	—
(iii) Rent of house property, situated in Kuwait but received in India	1,58,000	1,58,000	1,58,000
(iv) Profits from business in Nepal and deposited in bank there: Income accruing or arising outside India	12,000	—	—
(v) Income from profession in Oman which was set up in India, received there, managed from there: Foreign income accruing or arising outside India from a profession set up in India is taxable in case of ROR and RNOR. Its control and management is not relevant	1,70,000	1,70,000	—
(vi) Profit on sale of machinery in India but received in Italy: Income from asset situated in India is deemed to accrue or arise in India. Hence, it is taxable in all cases	1,26,000	1,26,000	1,26,000
(vii) Profits from foreign business: Depreciation of foreign business It can be set off first from business profits and thereafter against the income of any other head [Sec. 32(2)]	2,00,000 (-) 2,50,000	1,00,000 (-) 1,25,000	1,00,000 (-) 1,25,000
(viii) Income of a minor child is included in total income of that parent whose income, before including such income is greater [Sec. 64(1 A), however, an exemption up to Rs 1,500 is to be allowed under Sec. 10(32)]	1,68,500	1,68,500	1,68,500
(ix) Commission from German company received outside India is deemed to accrue or arise in India because of business connection in India [Sec. 9(1)(i)]	1,75,000	1,75,000	1,75,000
(x) Commission earned and received outside India on export orders collected in India is deemed to accrue or arise in India [Explanation 2 for Sec. 9(1)(i) w.e.f. AY (2007-2008)]	2,30,000	2,30,000	2,30,000
(xi) Dividends from foreign company received outside India	1,80,000	—	—
Total Income	17,69,500	16,22,500	14,52,500



Problem 6. Mr J, settled in Japan, comes back to India on 25 August 2011 to settle down here permanently. He purchased a house property on 2 October 2011. He started business on 1 November 2010. He disclosed the following incomes/outgoing during the financial year 2011-2012.

	₹
(i) Income from house property	2,25,000
(ii) Business profits	6,50,000
(iii) Loss from speculation business	1,85,000
(iv) Dividends from Japanese companies received there	1,60,000
(v) Profits from Japan business, controlled from India but received there	2,00,000
(vi) Deposit in public provident fund	40,000

Determine the residential status, total income for the previous year 2011-2012. Would you change your answer if house property is purchased on 1 October 2011?

Solution : (a) Determination of Residential Status for the PY 2011-2012.

Conditions of Part A - Sec.6(1)

Particulars	Previous year of house property, purchased on 2 October 2011			Previous year of business or profession, set up on 1 November 2011			Previous year of house property when it is acquired on 1 October 2011 instead of 2 October 2011.		
	Condition (a)	Condition (b)		Condition (a)	Condition (b)		Condition (a)	Condition (b)	
	Stay in India during PY 2011-12	(i) Stay in India during 4 years, preceding PY 2011-12	(ii) Stay in India during PY 2011-12	Stay in India during PY 2011-12	(i) Stay in India during 4 years, preceding PY 2011-12	(ii) Stay in India during PY 2011-12	Stay in India during 4 PY 2011-2012	(i) Stay in India during years, preceding PY 2011-12	(ii) Stay in India during PY 2011-12
Stay in India during the PY 2011-2012 and during 4 years preceding PY 2011-12 i.e. 2010-2011 to 2007-2008	181 days	Nil	181 days	151 days	Nil	151 days	182 days	Nil	182 days
Minimum stay required in India	182 days	365 days	60 days	182 days	365 days	60 days	182 days	365 days	60 days
Comment	Not satisfied	Not satisfied		Not satisfied	Not satisfied		Satisfied	Not satisfied	
Conclusion	Non-resident			Non-resident			Resident As additional two conditions of Sec. 6(6)(a) are not satisfied, he will be resident but not ordinarily resident.		

(b) Computation of total income for the PY 2011-2012:

Particulars of Income	Non-resident ₹	Resident not ordinarily resident ₹
(i) Income from house property	2,25,000	2,25,000
(ii) Profits and gains from business or profession:		
(a) Profits from Indian business	6,50,000	6,50,000
(b) Profits from Japan business, controlled from India but received there	—	2,00,000
(c) Loss from speculation business cannot be set off (Sec. 73). It will be carried forward to be set off against speculation business during next 4 assessment years.	—	—
(iii) Income from other sources: Dividend from Japanese company received there	—	—
Total Income	8,75,000	10,75,000
Less: Deduction u/s 80C— Deposit in PPF	(-) 40,000	(-) 40,000
Total Taxable Income	8,35,000	10,35,000

Problem 7. Determine the total income and tax liability of Mr. Karim taking following particulars into account:

Previous Year	2011-2012	2010-2011	2009-2010	2008-2009	2007-2008	2006-2007	2005-2006	2004-2005	2003-2004	2002-2003	2001-2002
Physically present in India (no. of days)	60	182	78	95	120	80	100	75	190	150	80

Particulars of total income :	₹
(i) Gross dividend received in Russia on 31 December 2011 from a company registered in India but mainly operating in Russia.	1,20,000
(ii) Pension from former employer in India received in Romania	1,50,000
(iii) Income from agriculture in Bhutan and received in India	20,000
(iv) Profits from a USA business, controlled from India but received there	3,00,000
(v) Profits from Delhi business, controlled from Pakistan, received in Pakistan	2,00,000
(vi) Dividends from a UK company, operating in India, received in UK	1,00,000
(vii) Gross salary for services rendered in Dhaka but received in Mumbai	50,000
Would you change your answer in the following cases:	
(i) During the previous year 2011-2012, she stays in India for 59 days instead of 60 days,	
(ii) During the previous year 2004-2005, she stays in India for 74 days instead of 75 days.	

Solution :

Particulars	Resident			Resident & ordinarily resident (ROR)/ Not ordinarily resident	
	Condition of Part A [Sec. 6(1)]			Conditions of Part B [Sec.6(6)(a)]	
	Condition (a)	Condition (b)			
	Stay in India during PY 2010-2011	(i) Stay in India during 4 years preceding PY	(ii) Stay in India during PY	Residential status in 10 years, preceding PY 2011-2012, i.e. 2010-2011 to 2001-2002	Stay in India during 7 years preceding PY 2011-2012, i.e. 2010-2011 to 2004-2005
Stay in India during the PY 2011-2012 and during 4 years preceding PY, i.e. 2010-2011 to 2007-2008	60 days	475	60	(i) Resident for 8 years 2001-2011 to 2003-2004 (ii) Non-resident for 2 years 2002-2003 and 2001-2002.	730 days
Minimum stay / Residential status required in India	182 days	365 days or more	60days or more	To be ROR, he should be resident in India at least for 2 years out of 10 years preceding the previous year and he should be in India at least for 730 days in 7 years preceding the PY, failing which he will be NOR.	
Comment	Not satisfied	Satisfied		Condition of ROR satisfied	

Workings: Resident status in 10 years preceding PY 2011-2012, i.e. 2010-2011 to 2001-2002.

S. No.	Previous Year	Stay in India in PY	Stay in India in 4 years preceding PY	Comment
1.	2010-2011	182 days	Not required	Resident
2.	2009-2010	78 days	395	Resident
3.	2008-2009	95 days	375	Resident
4.	2007-2008	120 days	445	Resident
5.	2006-2007	80 days	515	Resident
6.	2005-2006	100 days	495	Resident
7.	2004-2005	75 days	420	Resident
8.	2003-2004	190 days	Not required	Resident
9.	2002-2003	150 days	80 days	Non-resident
10.	2001-2002	80 days	Nil	Non-resident

Computation of total income

Particulars	Non-resident ₹	RNOR ₹	ROR ₹
(i) Income from salaries			
(a) Pension deemed to accrue or arise in India	1,20,000		
(b) Gross salary received in India	<u>1,50,000</u>		
	2,70,000	2,70,000	2,70,000
(ii) Income from business:	₹	₹	₹
(a) Agriculture income from Bhutan, received in India	20,000	20,000	20,000
(b) Profits from USA business/controlled from India but received in USA	-	3,00,000	3,00,000
(c) Profit from Delhi business, deemed to accrue or arise in India	2,00,000	2,00,000	2,00,000
(iii) Income from other sources			
(a) Dividend received in Germany from a domestic company is exempt [Sec. 10(34)]	—	—	—
(b) Dividend from a UK company, received in UK	—	1,00,000	—
Total Income	4,90,000	7,90,000	8,90,000

Problem 8. Kimono, a Japanese national discloses the following particulars of his income during financial year 2011-2012.

	₹
(i) Income from house property in Japan, remitted by tenant to him in India through State Bank of India	4,00,000
(ii) Loss from business in India	(-) 3,00,000
(iii) Profits from speculation business in India	2,00,000
(iv) Interest received on bonds of Indian companies outside India	1,45,000
(v) Net dividends received from Japanese companies outside India (tax deducted at source Rs 15,000)	2,35,000
(vi) Interest received on compensation of land, acquired by Government of India during the financial year 2006-2007	60,000
(vii) Profit from business in Japan, controlled and managed from India but being received in Japan	20,00,000

Determine his total income for the previous year 2011-2012 in the following cases :

- He is resident and ordinarily resident during the previous year;
- He is resident but not ordinarily resident during the previous year;
- He is non-resident during the previous year.

Solution : Computation of Total Income for PY 2011-2012

Particulars	Resident and ordinarily resident ₹	Resident but not ordinarily resident ₹	Non-resident ₹
(i) Income from house property in Japan received in India	4,00,000	4,00,000	4,00,000
(ii) Loss from business in India to be set off against business profits and thereafter against any other income except salary income and winning from lotteries/horse race etc. (Sec. 70)	(-) 3,00,000	(-) 3,00,000	(-) 3,00,000
(iii) Profits from speculation business in India	2,00,000	2,00,000	2,00,000
(iv) Profits from business in Japan, Rs 20,00,000 received outside India, control and management of foreign business in India is not relevant in the case of non-resident	20,00,000	20,00,000	—
(v) Interest on public sector companies in India deemed to accrue or arise in India though received outside India	1,45,000	1,45,000	1,45,000
(vi) Dividends of Rs 1,35,000 received from Japanese companies outside India, not accruing or deemed to accrue or arise in India	2,35,000	—	—
(vii) Interest for land compensation taxable on accrual basis: $60,000 \div 6 = [Rama Bai v. CIT (1991) 181 ITR 400 (S.C.)]$	10,000	10,000	10,000
Total Income	26,90,000	24,55,000	4,55,000

Problem 9. R discloses the following particulars of his income during the previous year 2011-2012 :

Particulars	₹
(i) Dividends from Sri Lankan companies received in India Dividends were received partly in cash and partly in shares. Face value of shares is Rs 80,000 but their market value is Rs 3,20,000. However, currently there is no buyer in the market	4,00,000
(ii) Pension remitted to him in India by Sri Lankan Government after deduction of tax source (Rs 15,000)	1,70,000
(iii) Fees received in Qatar for arguing a patent case in Delhi High Court on behalf of a fellow-lawyer friend of Mumbai	2,00,000
(iv) Commission credited to his account in India under his instructions by law firms in India, for referring clients from outside India but commission was received in Mauritius	1,00,000
(v) Share of income from his HUF, received in Kolkata	1,50,000
(vi) Income from law practice in Mauritius and Qatar, received there, but practice was set up in Delhi	6,80,000
(vii) 5% commission for the year 2011-2012 from publishers of law books on their annual profits, received in India, commission has been paid after setting off Rs 30,000 for books purchased by him. He has purchased the dealership rights from Mumbai Law House on 1 January 2012.	1,20,000
(viii) Gift from a foreign client, received outside India	20,000

Determine his total income for the previous year 2011-2012 if his residential status during the previous year is (i) ROR, or (ii) NOR or (iii) NR.

Solution : Computation of total income for PY 2011-2012 / AY 2012-2013

Particulars	ROR ₹	NOR ₹	NR ₹
(i) Dividend received in India			
(a) Cash dividend	80,000	80,000	80,000
(b) Dividend in kind to be valued at market price of shares ₹3,20,000	3,20,000	3,20,000	3,20,000
(ii) Pension received outside India and not deemed to accrue or arise in India [CIT v. Kalyanakrishnan 195 ITR 534]	1,70,000	—	—
(iii) Fees for arguing patent case in Delhi, but received in Ceylone—Income from business connection deemed to accrue or arise in India	2,00,000	2,00,000	2,00,000
(iv) Commission credited to the account of payee under his instruction in the books of payer is a deemed receipt [Raghava Reddy v. CIT (1962) 44 ITR 720 (SC)]	1,00,000	1,00,000	1,00,000
(v) Share income received from HUF exempt from tax [Sec. 10(2)]	—	—	—
(vi) Income from profession set up in India, extended outside India: Income being received outside India	6,80,000	6,80,000	—
(vii) Commission on account of dealership rights, received in India @ 5% or the annual profits of the publishers: Commission not to be apportioned between seller and purchaser on time basis	1,50,000	1,50,000	1,50,000
(viii) Gift from a foreign client, received outside India [Sec. 28(iv)]	20,000	—	—
Total Income	17,20,000	15,30,000	8,50,000

Problem 10. ABC & Co, is a partnership firm. It satisfies all conditions of the Income-tax Act. It discloses the following particulars of income for the previous year 2011-2012.

Particulars	₹
(i) Interest received in Egypt on monies lent to E Ltd., a company registered in Egypt, which utilised the borrowings in its business in India. 80% Business of E Ltd. is controlled from India	5,00,000
(ii) Royalty received in Paris from a cooperative society for using patent rights of the firm in its usiness in India, 30% affairs of the society are controlled from India	1,20,000
(iii) Income from house property in Bhutan, remitted to the firm in India through State Bank of India as per instructions of the firm	90,000
(iv) Interest on Development Bonds of Sri Lanka Government remitted to the firm in India through Bank of Ceylon	5,00,000
(v) Profit on sale of goods to a new customer in Myanmar, cargo documents were sent through Bank of Baroda	60,000
(vi) Profit on sale of goods FOB, to a customer in Malaysia, cargo documents were directly dispatched to him	1,00,000
(vii) Long-term capital gain received on sale of Bonds and Debentures of Indian companies in Myanmar, Bonds and Debentures were purchased in convertible foreign exchange. Capital gain, if computed in foreign currency will be 60% less than what it is in Indian currency	1,00,000
(viii) Under-writing commission for guaranteeing the public issue of a Malaysian company to be paid and received there subject to the condition that 20% commission will be paid either within 6 months from the end of the financial year Or within 3 months from the end of the month in which the approval of the Company Law Board is obtained, whichever period expires later	6,00,000

Determine the total income of the firm in the following case:

- (i) J is the managing partner of the firm. He controls the affairs of the firm from Malaysia.
- (ii) J comes to India for 182 days during the previous year. He has appointed K as his agent in Malaysia to take all decisions in his absence regarding affairs of firm. However, K has been directed to keep J fully informed while he is in India.
- (iii) J comes to India for 150 days. He has appointed K as his attorney to manage the affairs of firm in his absence in consultation with him.

Solution :

(a) Determination of residential status of the firm during PY 2011-2012:

Control and management of the firm is wholly situated outside India. The firm is non-resident in India. Physical presence of managing partner for 182 days in India during the previous year 2011-2012 is of no consequence. Situation (iii): Control and management is partly situated in India and partly outside India. The firm is “resident” in India during the previous year.

Computation of Total Income

Particulars	When firm is nonresident in India ₹	When firm is resident in India ₹
(i) Interest on loan-advances, made outside India, received outside India but loan was utilised for business in India, Accordingly, interest is deemed to accrue or arise in India	5,00,000	5,00,000
(ii) Royalty received in Paris from a cooperative society, for using using patent rights of the firm in its business in India. Royalty is deemed to accrue or arise in India	1,20,000	1,20,000
(iii) Income from house property in Bhutan, received by SBI in Bhutan as the agent of firm	—	90,000
(iv) Interest on Development Bonds of Sri Lanka Government remitted to the firm in India— Bank of Ceylon being agent of its Government	50,000	50,000
(v) Profit on sale of goods to a customer in Myanmar, title deeds sent to Bank of Baroda	—	60,000
(vi) Profits on sale of goods to a customer in Malaysia, cargo documents directly dispatched to the buyer— profit arises at seller's place	1,00,000	1,00,000
(vii) Capital gain on sale of bonds and debentures of Indian companies in Myanmar: It is deemed to accrue or arise in India	40,000	1,00,000
(viii) Under-writing commission 80% of Rs 6,00,000	—	4,80,000
Total Income	8,10,000	15,00,000

Problem 11. Compute Income for Mr. Jaikishan for the previous year 31-3-2012.

Particulars	₹
(a) Salary accrued and received in India	25,000
(b) Profit from hotel business in Japan	50,000
(c) Dividends declared in Japan received in India	10,000
(d) Gain from transfer of capital asset in India	25,000
(e) Interest on Debentures of a company in New York received in India	7,000
(f) Royalty received in Germany from a resident in India for technical services provided for a business in Germany	20,000



(g) Interest received in UK from Mr. Robert, a non-resident, on loan provided to him for business in India	
(h) Fees from an Indian company carrying on business in the UK for technical services rendered in London, directly deposited in his bank account in India.	6,000
Compute the total Mr. Jaikishan for the relevant assessment year, if he is	25,000
(i) Ordinarily resident,	
(ii) Not-ordinarily resident,	
(iii) Non-resident.	25,000

Solution : Computation of Total Income of Mr. Jaikishan for the assessment year 2012-2013

Particulars	ROR ₹	RNORs ₹	Non- resident ₹
(a) Salary accrued and received in India	25,000	25,000	25,000
(b) Profit from hotel business in Japan	50,000	—	—
(c) Dividends declared in Japan received in India	10,000	10,000	10,000
(d) Gains from transfer of a capital asset in India deemed to accrue or arise in India	25,000	25,000	25,000
(e) Interest on debentures of a company in New York but received in India	7,000	7,000	7,000
(f) Royalty received in Germany from a resident in India for technical services provided for a business in Germany	20,000	—	—
(g) Interest received in UK from Mr Robert, a non-resident, on loan provided on loan provided to him for business in India	6,000	6,000	6,000
(h) Fees from an Indian company, carrying on business in UK for technical services rendered in London, directly deposited in his book account in India	25,000	25,000	25,000
Total Income	1,68,000	98,000	98,000

Problem 12. Mr X furnishes the following particulars of his income earned during previous year 2011-12 :

- Income from agriculture in Bangladesh, received there ₹3,80,000, but later on remitted to India,
- Interest on Pakistani Development Bonds, ₹ 60,000, one-sixth of which received in India,
- Gift of ₹ 70,000 received in foreign currency from a relative in India,
- Arrears of salary ₹ 1,50,000 received in Pakistan from a former employer in India.
- Income from property received outside India ₹ 3,00,000 (₹ 1,00,000 is used in Bahrain for the educational expenses of his son in Bahrain, and ₹ 2,00,000 later on remitted to India).
- Income from business in Iran which is controlled from India (₹ 1,00,000 being received in India) ₹ 2,00,000.
- Dividends received on 30.06.2011 outside India from an Indian company, ₹ 2,50,000.
- Untaxed profit of the FY 2007-2008 brought to India in July 2010, ₹ 2,50,000.
- Profit (computed) on sale of building in India received in Pakistan ₹ 21,00,000.
- Profit from business in Kolkata managed from outside India ₹ 90,000, 60% of which is received outside India.

Find out gross total income of Mr. X for AY 2012-2013, if Mr. X is (a) resident and ordinarily resident; (b) resident but not ordinarily resident; (c) non-resident.

Solution : Computation of Gross Total Income for AY 2012-2013

Particulars	ROR ₹	RNORs ₹	Non- resident ₹
(i) Income from agriculture in Bangladesh, received there but later on remitted to India	3,80,000	—	—
(ii) Interest on Pakistan Development Bonds:			
1/6 th of ₹ 60,000 received in India	10,000	10,000	10,000
5/6 th of ₹ 60,000 being received in India	50,000	—	—
(iii) Gift received from a relative in India: Exempt [Sec. 57(v)]	—	—	—
(iv) Salary arrears received in Pakistan from a former employer in India	1,50,000	1,50,000	1,50,000
(v) Income from property received outside India but later on remitted to India	3,00,000	—	—
(vi) Profit from Iran business controlled from India:			
(a) Profits received in India	1,00,000	1,00,000	1,00,000
(b) Profits received outside India	1,00,000	1,00,000	—
(vii) Dividends received from an Indian company, outside India, deemed to accrue or arise in India but exempt under Sec. 10(34)	—	—	—
(viii) Untaxed foreign profit of PY 2007-2008 brought to India	—	—	—
(ix) Profit on sale of building in India, received outside India deemed to accrue or arise in India	21,00,000	21,00,000	21,00,000
(x) Profit from Kolkata business, managed from outside India: 60% received outside India	90,000	90,000	90,000
Gross Total Income	32,80,000	25,50,000	24,50,000



STUDY NOTE - 4

INCOME FROM SALARIES

This Study Note includes

- **Meaning of Salary**

Any person employed gets compensated by way of remuneration for services rendered. This is called 'Salary'. It is received in cash or in kind – by way of amenities, benefits, perquisites. Which emoluments are 'salary' how to value perquisites and what deductions are available from 'salary' has been dealt with under this head of income. In a recently enacted law, certain perquisites are taxed in the hands of 'employer' as Fringe Benefits Tax. Certain tax-free items of remuneration have been enumerated under section 10 and are discussed in this chapter.

4.1 MEANING OF SALARY

The meaning of the term 'salary' for purposes of income tax is much wider than what is normally understood. Every payment made by an employer to his employee for service rendered would be chargeable to tax as income from salaries. The term 'salary' for the purposes of Income-Tax Act will include both monetary payments (e.g. basic salary, bonus, commission, allowances etc.) as well as non-monetary facilities (e.g. housing accommodation, medical facility, interest free loans etc).

(1) Employer-employee relationship :

Before an income can become chargeable under the head 'salaries', it is vital that there should exist between the payer and the payee, the relationship of an employer and an employee.

(2) Full-time or part-time employment:

It does not matter whether the employee is a fulltime employee or a part-time one. Once the relationship of employer and employee exists, the income is to be charged under the head "salaries". If, for example, an employee works with more than one employer, salaries received from all the employers should be clubbed and brought to charge for the relevant previous years.

(3) Foregoing or Sacrificing of salary :

Once salary accrues, the subsequent waiver by the employee does not absolve him from liability to income-tax. Such waiver is only an application and hence chargeable.

(4) Surrender of salary :

However, if an employee surrenders his salary to the Central Government u/s 2 of the Voluntary Surrender of Salaries (Exemption from Taxation) Act, 1961, the salary so surrendered would be exempt while computing his taxable income.

(5) Salary paid tax-free :

This, in other words, means that the employer bears the burden of the tax on the salary of the employee. In such a case, the income from salaries in the hands of the employee will consist of his salary income and also the tax on this salary paid by the employer. This means both the salary and the tax paid thereon will be taxable in the hands of the employee.

(6) Voluntary payments :

Whether the payment from an employer is based on a contract or not, it constitutes salary in the hands of the employee. However, many employers give personal gifts and testimonials to the employees. For example, employees who complete 20 years of service may be given a wrist watch. The question arises whether the value of the watch can be taxed in the hands of the employee. Courts have taken the view that such gifts are not taxable. However, in these cases it is important that such gifts must be given to employees pursuant

to a scheme applicable to employees in general. If gifts are given purely on a selective basis they will become chargeable in the hands of the recipient. However, due to the levy of Fringe Benefit Tax, these gifts will now be exempt in the hands of the recipient, but will be taxable in the hands of the employer.

Sec.15: Year of Chargeability of Salary

- Due or receipt whichever falls earlier: Salary is taxable on due basis or on receipt basis, whichever is earlier. Hence,
 - (a) salary due in a previous year is taxable, even if it not received.
 - (b) Salary received in a previous year is taxable, even if it is not due.
 - (c) Arrears of salary received during the current previous year shall be taxable in the current year if not charged to tax in an earlier previous year.
- No double taxation: once salary is taxed on due/receipt basis, it will not be taxed again on receipt/falling due, as the case may be.
- The assessee can claim relief u/s 89(1) for arrears or advance salary.
- Loan from employer is not salary. Advance salary is taxable, while advance against salary is not taxable.
- For Government employees, the period of chargeability of salary is from March to February. For example, salary from 1st March 2008 to 29th February 2009 is chargeable as Income of the Assessment Year 2009-10.

“Place of accrual of salary”

- The place of accrual of salary is the place of employment.
- Service rendered in India: U/s 9(1)(ii), salary earned in India is deemed to accrue or arise in India even if –
 - (a) it is paid outside India,
 - (b) it is paid or payable after the contract of employment in India comes to an end.
- If an employee gets pension paid abroad in respect of services in India, the same will be deemed to accrue or arise in India
- Leave salary paid abroad in respect of leave earned in India is deemed to accrue or arise in India.
- Services rendered outside India: Sec.9(1)(iii) provides that income chargeable under the head “Salaries” payable by the Government to a citizen of India for service provided outside India will be deemed to accrue or arise in India.
- U/s 10(7), any allowance or perquisites paid or allowed outside India by the Government to a citizen of India for rendering services outside India will be fully exempted.

Items included under the head Salary u/s 17(1)

Salary includes:

- 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 salary
- Encashment of leave-not-availed
- Interest earned in excess of 9.5% on Recognized Provident Fund(RPF)
- Amount transferred in excess of 12% of Salary to RPF



- Contribution made by Central Government or any other employer (w.e.f. A.Y.2008-09) in the previous year to the account of an employee under Pension Scheme u/s 80 CCD.
- Money embezzled by an employee constitutes his income.

Profits in Lieu of Salary u/s 17(3)

- Compensation due or received from present/former employer in connection with
 - (a) termination of employment, or
 - (b) modification of terms and conditions of employment.
- Any amount received from an Unrecognized Provident Fund, to the extent of Employer's contributions, along with interest on such contribution.
- Sum received under Keyman Insurance Policy, including Bonus on it.
- Any sum received (either in lump sum or otherwise), either prior to employment or after cessation of employment.

Specified Employee

An Individual will be considered as a Specified Employee if :

- He is a director of a company, or
- He holds 20% or more of equity voting power in the company,
- Monetary salary in excess of ₹ 50,000: His income under the head salaries, (from any employer including a company) excluding non-monetary payments exceeds ₹ 50,000. For the above purpose, salary, should be arrived at after making the following deductions:
 - (a) Entertainment Allowance
 - (b) Professional Tax

TAXABILITY OF ALLOWANCES

Fully taxable allowances without any exemptions :

1. Basic Salary	9. Fees
2. Dearness Allowance	10. Lunch/Tiffin Allowance
3. Advance Salary	11. Overtime Allowance
4. Arrears of Salary	12. Servant Allowance
5. City Compensatory Allowance	13. Warden Allowance
6. Bonus	14. Non-practicing Allowance
7. Commission as a percentage on turnover	15. Family Allowance
8. Fixed Medical Allowance	16. Leave encashment during service

Specific allowances that are fully exempt in the hands of employees

Allowance	Conditions to claim full exemption
1. Travelling allowance	Should be provided by the employer and spent by the employee to meet the cost of official tour or transfer expenses. Cost of travel or transfer includes payments for transfer, packing and transportation of personal effects.
2. Daily Allowance	Should be spent by the employee for meeting the daily charges incurred on a tour or transfer.

3. Conveyance allowance	Should be used by the employee to meet the expenditure on conveyance in performance of official duties.
4. Helper allowance	Should be used by an employee to meet the expenditure on a helper who assists him in the performance of official duties.
5. Academic allowance	Should be used by the employee for his academic research and training pursuits.
6. Uniform allowance	Should be spent by the employee for purchasing/maintaining office uniform for official duties.
7. Allowances and perks paid by Government of India to an Indian citizen outside India	Fully exempted

Various items of Salary for which exemptions are available subject to limitations :

LEAVE TRAVEL ASSISTANCE (LTA) U/S 10(5) Rule 2B

Conditions for claiming the benefit:

- An individual can avail the benefit of LTA offered by his employer, twice in a block of four years.
- The present block of four years applicable for A.Y.2008-09 is calendar years 2006-2009.
- LTA may be provided by the employer to the employee and his family:
 - In connection with his proceeding on leave to any place in India, while in service.
 - Proceeding to any place in India after retirement or termination from service.

When Taxable :

- LTA encashed without performing journey is fully taxable
- Expenses reimbursed other than the fare like boarding or lodging is fully taxable.
- Amount received from employer in excess of the cost of traveling on the shortest route.

Family of an Individual means:

- Spouse and children of the individual, and
- Parents, brothers and sisters of the individual or any of them, wholly or mainly dependent on the individual.

HOUSE RENT ALLOWANCE [Sec. 10(13A) Rule 2A]

Conditions for claiming exemption:

- Assessee is in receipt of HRA
- Pays rent
- Rent paid is more than 10% of salary.

Very Important:

- The exemption shall be calculated on the basis of where the accommodation is situated.
- If the place of employment is the same for the whole year, then exemption shall be calculated for the whole year.
- If there is a change in place during the previous year, then it will be calculated on a monthly basis
- Exemption should be calculated in respect of the period during which rental accommodation is occupied by the employee during the previous year.
- Salary for the period during which rental accommodation is not occupied shall not be considered.

Salary for HRA= Basic Pay + DA(considered for retirement benefits) + Commission (if received as a fixed percentage on turnover as per terms of employment)

Taxable HRA:

Particulars	₹	₹
Amount received during the financial year for HRA		xxx
Less: Exemption u/s 10(13A) Rule 2A Least of the followings:		
(a) Actual amount received	xxx	
(b) 50% (for metro cities) / 40% of Salary (for other places)	xxx	
(c) Rent paid less 10% of Salary	xxx	xxx
Taxable HRA		xxx

OTHER ALLOWANCES

Allowances	Exemption u/s 10(14) Rule 2BB
Children Education Allowance	₹ 100 p.m.per child restricted upto 2 children
Children Hostel Expenditure Allowance	₹ 300 p.m.per child restricted upto 2 children
Running Allowance (for transport sector employees for meeting personal expenditure incurred during transport from one place to another)	Least of : (a) 70% of the amount received, or (b) ₹ 10,000 p.m.
Transport allowance (given to meet the employee's expenditure for traveling from his residence to office and back)	₹ 800 p.m. (in case of handicapped or blind employees, ₹ 1,600 p.m.)

GRATUITY

1. Government Employee: Fully exempted from tax u/s 10(10)(i).
2. Non-Govt.Employee:
 - (a) Employee **covered** by Payment of Gratuity Act,1972
Computation of Taxable Gratuity:

Particulars	₹	₹
Amount received as Gratuity		xxx
Less: Exemption u/s 10(10)(ii)		
Least of the followings:		
(i) Actual amount received	xxx	
(ii) $15/26 \times \text{Last drawn salary} \times \text{No. of years of completed service or part thereof in excess of 6 months}$	xxx	
(iii) Maximum Limit	10,00,000	xxx
Taxable Gratuity		xxx

Note: Salary = Basic Pay + Dearness Allowance

In case of seasonal employment, instead of 15 days, 7 days shall be considered.

- (b) Employee **not covered** by Payment of Gratuity Act,1972

Particulars	₹	₹
Amount received as Gratuity		xxx
Less: Exemption u/s 10(10)(iii)		
Least of the followings:		
(i) Actual amount receive	xxx	
(ii) $1/2 \times \text{Average salary} \times \text{No. of fully completed years of service}$	xxx	
(iii) Maximum Limit	10,00,000	xxx
Taxable Gratuity		xxx

Note: Salary = 10 months average salary preceeding the month of retirement.
 = Basic Pay + Dearness Allowance considered for retirement benefits + commission (if received as a fixed percentage on turnover)

Very Important :

- Where an individual receives retirement gratuity from more than one employer, he can claim exemption in respect of both of them.
- However, the maximum amount of exemption should not exceed ₹ 3,50,000
- When gratuity is received from more than one employer during different periods of time, the maximum exemption claimed by an assessee during his entire life should not exceed ₹ 3,50,000.

PENSION

1. Taxability of **Uncommuted Pension** or Monthly Pension:

- Pension is received periodically by the retired employee
- It may be received by Government or non-government employees
- Amount received shall be fully taxable under the head salaries

2. Taxability of **Commuted Pension**:

- Pension is received in lumpsum as per the terms of the employment on retirement or superannuation.
- Full Value of Commuted Pension = Amount received on commutation / percentage of commutation.
- Taxability:

Recipient	Amount Taxable
Government employee (Central/State/Local Authority or Statutory Corporation)	Fully exempted u/s 10(10A)(i)
Non-Govt. employee who has also received Gratuity u/s 10(10A)(ii)	Amount Received Less: 1/3 of Full Value of Commuted Pension
Non-Govt. employee who has not received Gratuity u/s 10(10A)(iii)	Amount Received Less: 1/2 of Full Value of Commuted Pension

LEAVE ENCASHMENT

- Leave encashment while in service is fully taxable as income of previous year in which it is encashed.
- Leave encashment on retirement: if an individual receives leave encashment on his retirement, then the amount received will be eligible for exemption. The amount of exemption is based on his employment:
 - Government employee: fully exempted from tax
 - Non-Govt. employee: An individual who is not a Government employee is also entitled for exemption in respect of Leave Encashment compensation received by him.

3. Computation of exemption from Leave Encashment:

Step 1 : Computation of Salary = 10 months average salary preceeding the month of retirement.

Step 2 : Salary = Basic Pay + Dearness Allowance (forming a part of salary for retirement benefits) + Commission (if received as a fixed percentage on turnover)

Step3 : This calculation is only applicable where the employer has sanctioned leave to the employee in excess of 30 days for every completed year of service.

Particulars	₹
(i) Leave credit available on the date of retirement	xxx
Less: Excess leave sanctioned by the employer (Leave sanctioned by the employer per year – 30 days per year) × No. of completed years of service)	xxx
Leave credit on the basis of 30 days credit for completed years of service	xxx
(ii) Leave salary on the basis of 30 days credit = Step 3(i) × Step 1	xxx

Note: In case the employer sanctioned leave of 30 days or less for completed year of service then the salary for actual leave balance shall be considered and Step 3(i) shall not apply.

4. Taxable Leave Salary on Retirement :

Particulars	₹	₹
Amount Received on Leave Encashment		xxx
Less: Exemption u/s 10(10AA)		
Least of the followings:		
(i) Actual amount of Leave encashment received	xxx	
(ii) Average salary of the individual for the past 10 months × 10 months	xxx	
(iii) Maximum Limit	3,00,000	
(iv) Leave at credit at the rate of 30 days p.a. for every Completed year of service as calculated in Step 3(ii)	xxx	xxx
Taxable Value of Leave Encashment		xxx

Note: (a) If the individual receives leave encashment from more than one employer, the quantum of exemption will be computed independently in respect of each employer.
(b) The total amount of exemption should not exceed ₹ 3,00,000 during his life time.

RETRENCHMENT COMPENSATION

Compensation is received by a workman at the time of:

- (i) closing down of the undertaking.
- (ii) transfer (irrespective of by agreement/compulsory acquisition) if the following conditions are satisfied:
 - service of workmen interrupted by transfer
 - terms and conditions of employment after transfer are less favourable
 - new employer is not under a legal obligation whether under the terms of transfer or otherwise to pay compensation on the basis that the employee's service has been continuous and has not been interrupted by transfer.

Note:

- (a) Retrenchment compensation received in accordance with any scheme, which is approved by the Central Government, is fully exempt from tax.
- (b) An individual who receives retrenchment compensation, is entitled for exemption u/s 10(10B).

Computation of Taxable Retrenchment Compensation :

Particulars	₹	₹
Amount received as Retrenchment Compensation		xxx
Less: Exemption u/s 10(10B):		
Least of the followings:		
(i) Actual amount received	xxx	
(ii) Amount determined under the Industrial Disputes Act, 1947	xxx	
(iii) Maximum Limit	5,00,000	xxx
Taxable Value		xxx

VOLUNTARY RETIREMENT COMPENSATION

Conditions for claiming exemption:

- An individual, who has retired under the Voluntary Retirement scheme, should not be employed in another company of the same management.
- He should not have received any other Voluntary Retirement Compensation before from any other employer and claimed exemption.
- Exemption u/s 10(10C) in respect of Compensation under VRS can be availed by an Individual only once in his lifetime.

Computation of Exemption:

Step 1: Salary = Last drawn salary = Basic Pay + D.A. (considered for retirement benefits)

Step 2: Taxable VRS compensation

Particulars	₹	₹
Amount received as VRS Compensation		xxx
Less: Exemption u/s 10(10C):		
Least of the followings:		
(i) Actual amount received	xxx	
(ii) Maximum Limit	5,00,000	
(iii) The highest of the following:		
• Last drawn salary $\times 3 \times$ No. of fully completed years of service		xxx
• Last drawn salary \times Balance of no. of months of service left.		xxx
Taxable Value		xxx

DEDUCTIONS AGAINST SALARY

1. Entertainment Allowance: Applicable only for Government Employees [Sec.16(ii)]

Least of the following will be allowed as a deduction:

- Actual amount of entertainment allowance received
- 20% of Basic salary of the Individual
- ₹ 5,000

2. Professional Tax [Sec.16(iii)]

- Professional tax or tax on employment paid by an employee, levied under a State Act shall be allowed as deduction



- (ii) such deduction is available only on actual payment
- (iii) If an employer pays professional tax on behalf of his employee, then it will first be included in the Salary as a perquisite and then, allowed as a deduction.

VALUATION & TAXABILITY OF PERQUISITES

Perquisite: Perquisite includes any amount due to or received in lump sum or otherwise by an assessee from an employer which is usually attached to a position.

Perquisite includes:

- (a) value of rent free accommodation given by the employer
- (b) value of accommodation given at concessional rate
- (c) value of benefit given free of cost or at concessional rate in the following cases:
 - given by employer to his Director Employee;
 - given by employer to his employee who owns 20% or more of voting power in the company, and
 - given by any employer (including company) to his employees whose monetary salary exceeds ₹ 50,000
- (d) any sum paid by the employer on behalf of the employees
- (e) sum paid/payable by the employer towards insurance on the life of the individual or annuity payments
- (f) Value of any other fringe benefit or amenity (excluding the fringe benefits chargeable to tax under Chapter XII-H as may be prescribed. [Sec.17(2)(vi)])

PERQUISITES WHICH ARE FULLY EXEMPTED FROM TAX

The following perquisites are exempt from tax in all cases and hence not includible for the purpose of tax deduction at source under section 192 during the financial year 2008-09:

1. Provision for medical facilities subject to limit
2. Tea or snacks provided during working hours
3. Free meals provided during working hours in a remote area or an offshore installation
4. Perquisites allowed outside India by the Government to a citizen of India for rendering service outside India.
5. Sum payable by an employer through a recognized provident fund or an approved superannuation or deposit-linked insurance fund established under the Coal Mines Provident Fund or the Employees Provident Fund.
6. Employer's contribution to staff group insurance scheme.
7. Leave travel concession subject to Sec.10(5)
8. Payment of annual premium by employer on personal accident policy effected by him on his employee
9. Free educational facility provided in an institute owned/maintained by employer to children of employee provided cost/value does not exceed ₹ 1,000 per month per child (no limit on no. of children)
10. Interest-free/concessional loan of an amount not exceeding ₹ 20,000
11. Computer/laptop given(not transferred) to an employee for official/personal use.
12. Transfer without consideration to an employee of a movable asset (other than computer, electronic items or car) by the employer after using it for a period of 10 years or more.
13. Traveling facility to employees of railways or airlines.
14. Rent-free furnished residence (including maintenance thereof) provided to an Official of Parliament, a Union Minister or a Leader of Opposition in Parliament.
15. Conveyance facility provided to High Court Judges u/s22B of the High Court Judges (Conditions of Service) Act,1954 and Supreme Court Judges u/s 23A of the Supreme Court Judges (Conditions of Service) Act,1958.

16. Conveyance facility provided to an employee to cover the journey between office and residence.
17. Accommodation provided in a remote area to an employee working at a mining site or an onshore oil exploration site, or a project execution site or an accommodation provided in an offshore site of similar nature.
18. Accommodation provided on transfer of an employee in a hotel for not exceeding 15 days in aggregate.
19. Interest free loan for medical treatment of the nature given in Rule 3A.
20. Periodicals and journals required for discharge of work.
21. Tax on perquisite paid by employer [Sec.10(10CC)]
22. Other Exempted Payments:
 - Bonus paid to a football player after the World Cup victory to mark an exceptional event
 - Payment made as a gift in appreciation of the personal qualities of the employee.
 - Payment of proceeds of a benefit cricket match to a great cricket player after he retired from test match.
 - Trust for the benefit of employee's children.

MEDICAL FACILITIES

- Fixed medical allowance is fully taxable
- Medical payments include reimbursements also [circular no.603/6.6.1991]

MEDICAL TREATMENT IN INDIA

1. Local treatment to employee or any member of his family in:

- Hospital maintained by employer
- Government Hospital
- Notified hospital for prescribed diseases [Sec.17(2)(v)]

Family includes spouse, children (whether dependent or independent) and parents, brothers and sisters wholly dependent on the employee.

2. Group Medical insurance paid u/s 36(1)(ib) & Medical Insurance paid u/s 80D- which are approved by the Central Govt. or IRDA w.e.f. A.Y.2007-08.
3. Any other medical expenditure reimbursed subject to a maximum of ₹ 15,000

MEDICAL TREATMENT ABROAD (for the patient and the attendant)

If the employee underwent medical treatment abroad and the expenditure is met by the employer, the exemption will be subject to the following:

1. Medical treatment and stay expenses abroad(both for the patient and the attendant) is exempt from tax, subject to the maximum amount permitted by the Reserve Bank of India.
2. Travel expenditure of the patient and the attendant:

Gross Total Income, before including reimbursement of Foreign Travel Expenditure	Amount of Exemption
Upto ₹ 2,00,000	Fully exempted
Above ₹ 2,00,000	Fully taxable

3. Computation of exemption for foreign travel expenditure

- Step 1:** Compute Gross Total Income of the assessee without considering foreign travel reimbursement but after set-off loss and unabsorbed depreciation.
- Step 2:** If the Gross Total Income does not exceed ₹ 2 lakhs, Foreign Travel Reimbursement is not taxable otherwise fully taxable.

Step 3: If Foreign Travel reimbursement is taxable as per Step 2, recomputed the income under the head Salary after including foreign travel reimbursement and Gross Total Income must also be recomputed.

ACCOMMODATION FACILITIES

1. Value of Unfurnished Accommodation: Explanation 1 to Sec.17(2), Rule 3(1)

Nature of Perquisite	Taxable Value of Perquisite
Provided by Central Govt. or State Govt.	Licence fee determined by the Government Less: Rent recovered from employee

Provided by Employer other than Central or State Government

(a) owned by employer	In cities having population exceeding 25 lakhs as per 2001 census: 5% of Salary Less Rent actually paid by employee In cities having population exceeding 10 lakhs but not exceeding 25 lakhs as per 2001 census: 10% of Salary Less Rent actually paid by employee In other places: 7.5% of Salary Less Rent actually paid by employee
(b) taken on lease by the employer	Rent paid by the employer or 15% of Salary whichever is lower Less Rent recovered from employee
(c) Accommodation in a hotel	24% of salary paid/payable or actual charges paid/payable whichever is lower Less Amount paid or payable by the employee

Hotel Accommodation : Accommodation provided in a hotel will not be a taxable perquisite if the following two conditions are fulfilled:

- The period of such accommodation does not exceed 15 days
- Such accommodation has been provided on the transfer of the employees from one place to another.

2. Value of Furnished Accommodation

Particulars	₹
Value of unfurnished accommodation as above	xxx
Add : Value of Furniture provided: <ul style="list-style-type: none"> • If owned by employer, 10%p.a. of original cost of such furniture • If hired from third party, then Actual hire charges 	xxx
Less: Any charges paid or payable by the employee	(xxx)
Value of Furnished Accommodation	xxx

Note : Furniture includes Television sets, radio, refrigerator, other household appliance, air-conditioning plant or equipment.

3. Valuation not applicable:

- Employees working at mining site, onshore oil exploration site, offshore site, project execution site, dam site, power generation site.
- Conditions to be fulfilled:
 - The accommodation should be of a temporary nature, and
 - Plinth area should not exceed 800 square feet

- Accommodation should be located at least 8 kms away from local limits of municipality/cantonment or located in a remote area

Remote area means area located at least 40 kms away from town having a population not exceeding 20,000 based on latest published All-India census.

4. Valuation of accommodation in case of Employees on transfer :

- For the first 90 days of transfer: Where accommodation is provided both at existing place of work and in new place, the accommodation, which has lower value, shall be taxable.
- After 90 days : Both accommodations shall be taxable.

5. Salary for Valuation of Accommodation facilities :

Salary includes	Salary excludes
<ul style="list-style-type: none"> • Basic Salary • D.A. (if considered for retirement benefits) • All taxable allowances • Bonus or commission or ex-gratia • Any other monetary payment 	<ul style="list-style-type: none"> • Other D.A • Employer's contribution to PF • Exempted allowances • Perquisites u/s 17(2) • Perquisites u/s 17(2)(iii) or its provisions

OTHER FACILITIES AND PERQUISITES TO EMPLOYEE AND HIS HOUSEHOLD

Rule	Nature of Perquisite	Taxable Value of Perquisite(TVP)
3(3)	Service of sweeper, gardener or watchman or personal attendant	Actual cost to the employer Less: Amount paid by employee
3(4)	Supply of gas, electricity or water for household consumption	Procured from outside agency Amount paid to outside agency Resources owned by employer himself Manufacturing cost per unit Less: amount paid by the employee
3(5)	Education facilities to members of his household (a) free education to children in the school maintained by the employer or the school sponsored by the employer (b) other schools (c) for other members of the household	If the cost of education per child does not exceed ₹ 1,000 p.m.- then not taxable For points (b) & (c) In other case, cost to the employer Less: amount recovered from employee
3(7)(i)	Housing Loan/Vehicle Loan- for acquiring capital assets and not for repairs. SBI Rate= SBI Rate prevailing on the first day of the previous year	Other Loans Interest charged by employer is equal to or higher than SBI rates. It is not a taxable perquisite Interest charged is lower than SBI rates: Interest charged at SBI rates on maximum outstanding balance Less: Interest paid by the employee on that loan Similar treatment as above. Exceptions : (a) Medical loan for treatment of diseases specified in Rule 3A except loan reimbursed by medical insurance (b) Loan not exceeding ₹ 20,000 in aggregate 3(7)(vii)
Use of	any movable asset other than computer or laptops or other assets already mentioned 10% of Actual Cost if owned by the employer; or Actual rental charge paid/payable by the employer	Less: Amount recovered from employee

TRANSFER OF MOVABLE ASSETS TO EMPLOYEES [Rule 3(7)(viii)]

Particulars	Computer & Electronic Gadgets	Car	Other Movable Assets
Method of Depreciation	WDV	WDV	SLM
Rate of Depreciation for every completed year	50%	20%	10%
Actual Cost	XXXXXX	XXXXXX	XXXXXX
Less : Depreciation for completed years	(XXXXXX)	(XXXXXX)	(XXXXXX)
WDV at the end of completed years	XXXXXX	XXXXXX	XXXXXX
Less : Sale Value taken from Employee	(XXXXXX)	(XXXXXX)	(XXXXXX)
Taxable Value of Perquisite	XXXXXX	XXXXXX	XXXXXX

Note :

- Electronic gadgets include computer, digital diaries and printers, but excludes washing machines, microwave ovens, hot plates, mixers, ovens, etc.
- Transfer of Assets, which are 10 years old, shall not attract tax liability.
- Member of household includes: Spouse(s), children and their spouses, parents, servants and dependents.
- Completed year means actual completed year from the date of acquisition of the asset to the date of transfer of such asset to the employees.

TAXABILITY OF PERQUISITES PROVIDED BY EMPLOYERS
Taxability of Motor Car Benefits

Owner of Car	Expenses borne by	Purpose	Taxable Value of Perquisite
1(a) Employer	Employer	Fully official	Not a perquisite provided the documents as specified in Rule 3(2)(B) are maintained.
1(b) Employer	Employer	Fully private	Total of: (i) Actual expenditure on car (ii) Remuneration to chauffeur (iii) 10% of the cost of car (normal wear & tear) Less: Amount charged from employee
1(c)(i) Employer	Employer	Partly official and partly personal	<u>Cubic Capacity of Car Engine upto 1.6 litres</u> ₹ 1,800 p.m.+ ₹ 900 p.m. for chauffeur <u>Cubic Capacity of Car Engine above 1.6 litres</u> ₹ 2,400 p.m. + ₹ 900 p.m. for chauffeur
1(c)(ii) Employer	Employee	Partly for official and partly for personal	<u>Cubic Capacity of Car Engine upto 1.6 litres</u> ₹ 600 p.m + ₹ 900 p.m. for chauffeur <u>Cubic Capacity of Car Engine above 1.6 litres</u> ₹ 900 p.m. + ₹ 900 p.m. for chauffeur

Owner of Car	Expenses borne by	Purpose	Taxable Value of Perquisite
2(i) Employee	Employer	Fully official use	Not a perquisite provided the documents as specified in Rule 3(2)(B) are maintained.
2(ii) Employee	Employer	Partly official and partly personal	Subject to Rule 3(2)(B) Actual expenditure incurred. Less: Car cubic capacity upto 1.6 litres [i.e. value as per 1(c)(i)] OR Car cubic capacity upto 1.6 litres above 1.6 litres [i.e. value as per 1(c)(i)]
3(i) Employee owns other auto-motive but not car	Employer	Fully official use	Not a perquisite provided the documents as specified in Rule 3(2)(B) are maintained.
3(ii) Employee owns other auto-motive but not car	Employer	Partly for official use	Subject to Rule 3(2)(B) Actual expenditure incurred by employer. Less: ₹ 900 p.m.

Note :

1. Using cars from pool of cars owned or hired by Employer:

The employee is permitted to use any or all cars for both official and personal use:

For one car	Valued as per 1(c)(i)
For more than one car	Valued as per 1(b) as if fully used for personal purpose

2. Documents to be maintained for claiming 'not taxable perquisite' or higher deduction wherever applicable [Rule 3(2)(B)]

- Employer should maintain complete details of journey undertaken for official purpose, which includes date of journey, destination, mileage and amount of expenditure incurred thereon.
- Certificate of supervising authority of the employee, wherever applicable, to the effect that the expenditure incurred for wholly and exclusively for performance of official duties, should be provided.

TAXABILITY OF OTHER BENEFITS

Rule	Nature of Perquisite	Taxable Value of Perquisite (TVP)
3(6)	Transportation of goods or passengers at free or concessional rate provided by the employer engaged in that business (other than railways/ airlines)	Value at which offered to public Less: amount recovered from the employee
3(7)(ii)	Traveling, touring, accommodation and other expenses met by the employer other than specified in Rule 2B. (this shall be calculated only for the period of vacation)	Amount recovered by employer or Value at which offered to public Less: amount recovered from the employee
3(7)(iii)	Free meals during office hours Free meal in remote area or offshore installation area is not a taxable perquisite	Actual cost to the employer in excess of ₹ 50 per meal or tea or snacks Less: amount recovered from the employee. Tea or non-alcoholic beverages and snacks during working hours is not taxable.

Rule	Nature of Perquisite	Taxable Value of Perquisite (TVP)
3(7)(iv)	Value of any gift or voucher or taken other than gifts made in cash or convertible into money (e.g. gift cheques) on ceremonial occasion	Value of gift In case the aggregate value of gift during the previous year is less than ₹ 5,000 , then it is not a taxable perquisite
3(7)(v)	Expenditure incurred on credit card or add on card including membership fee and annual fee	Actual expenditure to employer is taxable Less: amount recovered from employee If it is incurred for official purpose and supported by necessary documents then it is not taxable.
3(7)(vi)	Expenditure on club other than health club or sports club or similar facilities provided uniformly to all employees	Actual expenditure incurred by the employer Less: amount recovered from employee If the expenditure is incurred exclusively for official purposes and supported by necessary documents then it is not taxable. Initial fee of corporate membership of a club is not a taxable perquisite
3(7)(ix)	Any other benefit or amenities or service or right or privilege provided by the employer other than telephone or mobile phone	Cost to the employer Less: amount recovered from employee

Note: Members of household includes: spouse(s), children and their spouses, parents, servants and dependents.

PROVIDENT FUNDS

Particulars	Statutory	Recognized	Unrecognized	Public
Constituted under	Provident Funds Act, 1952	EPF and Misc, Provisions Act, 1952 & recognized by the Commissioner of PF and CIT	Not recognized by the Commissioner of Income Tax	Public Provident Fund Act, 1968 Account in SBI or Post Offices
Contribution by	Employer and Employee	Employer and Employee	Employer and Employee	All assessee's independently
Assessee's Contribution	Deduction u/s 80C	Deduction u/s 80C	No Income Tax Benefit	Deduction u/s 80C
Employer's Contribution	Not taxable	Amount exceeding 12% of salary is taxable	Not taxable at the time of contribution	Not applicable
Interest credited	Fully exempted	Exempted upto 9.5% p.a. Any excess is taxable	On Employee's contribution taxable under the head "Other Sources" On Employer's contribution not taxable at the time of credit	Fully exempt
Withdrawal at the time of retirement/resignation/termination, etc	Exempted u/s 10(11)	Exempted u/s 10(12) Subject to conditions	Employee's contribution and interest thereon is not taxable. Employer's contribution and interest thereon is taxable as Profits in lieu of Salary, under "Salaries"	Exempted u/s 10(11)

Note: Sum received by an Employee under approved Superannuation Fund is also exempt from tax u/s 10(13).

EMPLOYERS CONTRIBUTION TO RPF IS EXCLUDED FROM SALARY

1. If the employee has rendered continuous service with his employer for a period of 5 years or more.
2. If he has not rendered such continuous service of 5 years, then the service has been terminated:
 - (a) by reason of such employee's ill health, or
 - (b) by the contraction or discontinuance of the employer's business, or
 - (c) any other cause beyond the control of the employee
3. If, on the cessation of his employment, the employee obtains employment with another employer, to the extent, the accumulated balance due and becoming payable to him is transferred to his individual account in any recognized fund maintained by such employer.

The period of service rendered under the previous employer(s) should also be included in determining the period of continuous service in (3) above.

TAXABILITY OF PERQUISITES (At a glance)

Perquisites	Specified Employee	Non-specified Employee
Rent free/concessional accommodation	Taxable	Taxable
Watchman, gardener, sweeper, personal attendan engaged by employee and expenses met by the employer	Taxable	Taxable
The aforesaid mentioned servants provided in any other manner	Taxable	Non-taxable
Gas, electricity, water, etc. for household consumption and the connection in the name of employee but expenses paid by the employer	Taxable	Taxable
Above facilities provided in any other manner	Taxable	Non-taxable
Education expenses, if the bills are in the name of employee, the but met by employer	Taxable	Taxable
Above facilities provided in any other manner	Taxable	Non-taxable
Transport facility provided by transport undertakings Railways and other than Airlines	Taxable	Taxable
Interest free loans or loans provided at concessional rates by the employer to employee	Taxable	Taxable
Holiday home facilities provided	Taxable	Taxable
Club facility provided by employer(other than official purposes)	Taxable	Taxable
Computer/laptop provided by the employer for use by the employee	Non-taxable	Non-taxable
Other movable assets provided by the employer for use by the employees	Taxable	Taxable
Sale/transfer of movable assets to employees	Taxable	Taxable
Magazines, periodicals, journals, etc. for official work	Not taxable	Not taxable
Medical facilities, if the bills are in the name of employee, employer upto but met by ₹ 15,000	Taxable	Taxable
Above facility in any other manner	Taxable	Non-taxable
Leave Travel Concession	Not taxable subject to Sec.10(5)	Not taxable subject to Sec.10(5)
Stock option under approved scheme	Not taxable	Not taxable

SALARY

For the purpose of	Means
1. Deduction for Entertainment Allowance u/s 16(ii) in case of Govt. employees	Basic pay
2. Voluntary Retirement Compensation u/s 10(10C)	Basic Pay + D.A. (forming part of salary for retirement benefits)
3. Exemption for Gratuity covered under Payment of Gratuity Act u/s 10(10)(ii)	Basic Pay + D.A.
4. Exemption for Gratuity not covered under Payment of Gratuity Act u/s 10(10)(iii) fixed percentage on turnover	Basic Pay + D.A. (forming part of salary for retirement benefits) + Commission as a
5. Exemption for Leave Salary u/s 10(10AA)	Same as above
6. Exemption for House Rent Allowance u/s 10(13A)	Same as above
7. Contribution to Recognized Provident Fund	Same as above
8. Determination of Specified employee u/s 17 including the value of non-monetary	Income under the head salaries without benefits
9. Rent-free accommodation	Salary includes
Salary excludes	<ul style="list-style-type: none"> • Basic pay • D.A. (not forming part of salary)
• D.A. (forming part of salary)	
• Employer's contribution to PF	• Exempted allowances
• All taxable allowances	
• Bonus or commission or ex-gratia	• Perquisites u/s 17(2) or (2)(iii) or its provisions
• Any other monetary payment	• Any allowance in the nature of medical facility to the extent not taxable.

ILLUSTRATIONS ON INCOME FROM SALARIES

Illustration 1. Mr.Z has joined ICC Ltd. on 1st July 2008 in the scale of ₹15,000-1,500-21,000-2,500-31,000. Compute gross salary for the previous year 2011-12.

Solution :

Previous Year: 2011-12

Salary for (i) April 2011 to June 2011 = $18,000 \times 3 =$ 54,000
(ii) July 2011 to March 2012 = $19,500 \times 9 =$ 1,75,500

Gross Salary 2,29,500

Workings:

Previous Year	April to June	July to March
2008-09	Nil	15,000
2009-10	15,000	16,500
2010-11	16,500	18,000
2011-12	18,000	19,500

Illustration 2. Mr.Kabir is getting a salary of ₹12,000 p.m. w.e.f. 1.4.2010. He is promoted w.e.f. 31.12.2010 and got arrears of ₹75,000. Bonus for the year 2011-12 is ₹ 15,000 remains outstanding but bonus of ₹ 12,000 for the year 2010-11 was paid on 1st January 2012. In March 2012, he got two months salary i.e. April and May 2012 in advance. Compute the gross salary for the assessment year 2012-13.

Solution :

Computation of Gross Salary for the Assessment Year 2012-13

Salary : ₹ 12,000 × 12 1,44,000
Arrears of Salary 75,000
Bonus for the year 2011-12 : (Receivable) —
Bonus for the year 2010-11 : (Received) 12,000
Advance of Salary: April & May 2012 ($12,000 \times 2$) 24,000
Gross Salary 2,55,000

Illustration 3. Mr.Pradip, a foreign technician is employed with an Indian company. His contract of service was approved by the Government. He was in receipt of bonus from the said Company where he is working. The Assessing Officer subjected the amount to tax on the ground that bonus receipt falls outside the purview of the contract of service. Is the Assessing Officer justified?

Solution : U/s 9(1)(ii) salary earned in India is deemed to accrue or arise in India and is taxable in India.

The salary and bonus paid to a foreign technician for services rendered in India is taxable in India and the same is not entitled for any exemption from the Assessment Year 2008-09 onwards.

Illustration 4. Amal Kumar, an Indian citizen, is posted in the Indian High Commission at Nairobi during the previous year 2011-12.

His emoluments consist of Basic Pay of ₹1,50,000 per month and overseas allowance of ₹ 60,000 per month. Besides, he is entitled to & fro journey to India and also use Government's car at Nairobi. He has no taxable income except salary income stated above.

Compute tax liability if (i) he is a non-resident during the previous year 2011-12 and (ii) he is a foreign citizen.

Solution :

- (1) U/s 9(1)(iii), Salary paid by the Government of India to an Indian citizen for services rendered outside India is deemed to accrue or arise in India and is therefore taxable in India.
- (2) U/s 10(7), allowances or perquisites paid by the Government of India to an Indian citizen or services rendered outside India, is fully exempt from tax.

(3) Computation of Taxable Salary for the Previous Year 2011-12

Particulars	Rs	Rs
Salary (1,50,000 × 12)		18,00,000
Overseas Allowance (60,000 × 12)	7,20,000	
Less: Exempt u/s 10(7)	<u>7,20,000</u>	<u>Nil</u>
Gross Salary		18,00,000
Less: Deduction u/s 16		<u>Nil</u>
Income under the head Salaries		18,00,000

HOUSE RENT ALLOWANCE [Sec.10(13A) Rule 2A]

Illustration 5. A, is entitled to a basic salary of ₹5,000 p.m. and dearness allowance of ₹1,000 p.m., 40% of which forms part of retirement benefits. He is also entitled to HRA of ₹2,000 p.m. He actually pays ₹2,000 p.m. as rent for a house in Delhi. Compute the taxable HRA.

Solution :

Salary for HRA= Basic Pay + D.A. (considered for retirement benefits) + Commission (if received as a fixed percentage on turnover as per terms of employment) = (5,000 × 12) + (40% × 1,000 × 12) = 64,800

Taxable HRA :

Particulars	₹	₹
Amount received during the financial year for HRA		24,000
Less: Exemption u/s 10(13A) Rule 2A Least of the followings:		
(a) Actual amount received	24,000	
(b) 50% of Salary of ₹64,800	32,400	
(c) Rent paid less 10% of Salary [2,000 × 12 – 10% of 64,800]	17,520	17,520
Taxable HRA		6,480

Illustration 6. X, is employed at Delhi as Finance Manager of R Ltd. The particulars of his salary for the previous year 2011-12 are as under: Basic Salary ₹16,000 p.m.. Dearness allowance ₹12,000 p.m. Conveyance Allowance for personal purpose ₹2,000 p.m.; Commission @2% of the turnover achieved which was ₹9,00,000 during the previous year and the same was evenly spread. HRA ₹6,000 pm. The actual rent paid by him ₹5,000 pm for an accommodation at till 31.12.11. From 1.1.12 the rent was increased to ₹7,000 pm. Compute taxable HRA.

Note : If there is an increase in rent paid, it is advisable to calculate the exemptions separately based on the time period. Rent before and after increase.

Solution :

Salary for HRA (for 9 months)= Basic Pay + DA(considered for retirement benefits) + Commission (if received as a fixed percentage on turnover as per terms of employment)

$$= (16,000 \times 9) + (12,000 \times 9) + (2\% \text{ of } 9,00,000 \times 9/12) = 2,65,500$$

Taxable HRA: (April to December 2011). Total time=9 months

Particulars	₹	₹
Amount received during the financial year for HRA		54,000
Less: Exemption u/s 10(13A) Rule 2A.		
Least of the followings:		
(a) Actual amount received	54,000	
(b) 50% of Salary	1,32,750	
(c) Rent paid less 10% of Salary [5,000 × 9 – 10% of 2,65,500]	18,450	18,450
Taxable HRA		35,550

Salary for HRA (for 3 months)= Basic Pay + DA(considered for retirement benefits) + Commission (if received as a fixed percentage on turnover as per terms of employment)
 $= (16,000 \times 3) + (12,000 \times 3) + (2\% \text{ of } 9,00,000 \times 3/12) = 88,500$

Taxable HRA :

Particulars	Rs	Rs
Amount received during the financial year for HRA		18,000
Less: Exemption u/s 10(13A) Rule 2A		
Least of the followings:		
(a) Actual amount received	18,000	
(b) 50% of Salary	44,250	
(c) Rent paid less 10% of Salary [7,000 × 3 – 10% of 88,500]	12,150	12,150
Taxable HRA		5,850

Illustration 7. Z is employed in A Ltd. As on 31.3.11, his basic salary ₹ 6,000 p.m. He is also entitled to a dearness allowance of 50% of basic salary. 70% of the dearness allowance is considered for retirement benefits. The company gives him HRA ₹ 3,000pm. With effect from 1.1.11 he receives an increment of ₹ 1,000 in his basic salary. was staying with his parents till 31.10.2011. From 1.11.10 he takes an accommodation on rent in Delhi and pays ₹ 2,500 pm as rent for the accommodation. Compute taxable HRA for the assessment year 2012-13.

Solution :

Salary for the purpose of HRA shall cover the time period for which the assessee, who is in receipt of HRA, resided in a rented accommodation and the rent paid by such assessee, is more than 10% of salary.

Salary for HRA (for 5 months) = Basic Pay + DA (considered for retirement benefits) + Commission (if received as a fixed percentage on turnover as per terms of employment)

Basic Pay = $(5,000 \times 2) + (6,000 \times 3) = 28,000$

DA = 50% of Basic Pay × 70% forming part of retirement benefits
 $[50\% \times 28,000 \times 70\%] = 9,800$

Total Salary for HRA **37,800**

Taxable HRA :

Particulars	₹	₹
Amount received during the financial year for HRA $(3,000 \times 12)$		36,000
Less: Exemption u/s 10(13A) Rule 2A.		
Least of the followings:		
(d) Actual amount received	36,000	
(e) 50% of Salary	18,900	
(f) Rent paid less 10% of Salary [2,500 × 5 – 10% of 37,800]	8,720	8,720
Taxable HRA		27,280

GRATUITY

Illustration 8. Mr. Hari retires on 15th October 2011, after serving 30 years and 7 months. He gets ₹3,80,000 as gratuity. His salary details are given below:

FY 2011-12	Salary ₹16,000 pm	D.A. 50% of salary. 40% forms part of retirement benefits.
FY 2010-11	Salary ₹15,000 pm	D.A. 50% of salary. 40% forms part of retirement benefits

Determine his gross salary in the following cases:

- He retires from government service
- He retires from seasonal factory in a private sector, covered under Payment of Gratuity Act, 1972.
- He retires from non-seasonal factory, covered by Payment of Gratuity Act, 1972
- He retires from private sector, not covered by payment of Gratuity Act

Solution :

- The amount of gratuity received as a Government employee is fully exempt from tax u/s 10(10)(i)
- As an employee of a seasonal factory, in a private sector, covered under the Payment of Gratuity Act, 1972

Computation of Taxable Gratuity

Particulars	₹	₹
Amount received as Gratuity		3,80,000
Less: Exemption u/s 10(10)(ii)		
Least of the followings:		
(i) Actual amount received	3,80,000	
(ii) $7/26 \times$ Last drawn salary \times No. of years of completed service or part thereof in excess of 6 months $[31 \times 7/26 \times 24,000]$	2,00,308	
(iii) Maximum Limit	10,00,000	2,00,308
Taxable Gratuity		1,79,692

- As an employee of a non-seasonal factory, covered by Payment of Gratuity Act, 1972

Computation of Taxable Gratuity

Particulars	₹	₹
Amount received as Gratuity		3,80,000
Less: Exemption u/s 10(10)(ii)		
Least of the followings:		
(i) Actual amount received	3,80,000	
(ii) $15/26 \times$ Last drawn salary \times No. of years of completed service or part thereof in excess of 6 months $[15/26 \times 31 \times 24,000]$	4,29,231	
(iii) Maximum Limit	10,00,000	3,80,000
Taxable Gratuity		NIL

Note : Salary = Basic Pay + Dearness Allowance

In case of seasonal employment, instead of 15 days, 7 days shall be considered.

(iv) As an employee of a private sector, not covered by Payment of Gratuity Act, 1972

Computation of Taxable Gratuity

Particulars	₹	₹
Amount received as Gratuity		3,80,000
Less: Exemption u/s 10(10)(iii) Least of the followings:		
(i) Actual amount received	3,80,000	
(ii) $1/2 \times \text{Average salary} \times \text{No. of fully completed years of service}$ $[\frac{1}{2} \times 18,720 \times 30]$	2,80,800	
(iii) Maximum Limit	10,00,000	2,80,800
Taxable Gratuity		99,200

Note: Salary = 10 months average salary preceeding the month of retirement.

= Basic Pay + Dearness Allowance considered for retirement benefits + commission
(if received as a fixed percentage on turnover)

Salary for the months December '10 till September '11 shall have to be considered.

Basic Salary:	₹
December '10 to March '11 = $15,000 \times 4$	= 60,000
April '11 to September '11 = $16,000 \times 6$	= 96,000
Total Basic Salary	1,56,000
Add: D.A. [50% of 1,56,000 \times 40%, forming part of superannuation benefits]	31,200
Salary for 10 months	1,87,200

Therefore, **Average salary for 10 months = $1,87,200/10 = 18,720$**

Illustration 9. Mr.Surya was an employee of Z Ltd. After 38 years of service, he retired on 28.2.12. He was drawing a monthly salary of ₹18,000. On retirement he received a gratuity of ₹4,00,000. Compute taxable gratuity.

Solution : Assuming employee **not covered** by Payment of Gratuity Act, 1972

Computation of Taxable Gratuity

Particulars	₹	₹
Amount received as Gratuity		4,00,000
Less: Exemption u/s 10(10)(iii) Least of the followings:		
(i) Actual amount received	4,00,000	
(ii) $1/2 \times \text{Average salary} \times \text{No. of fully completed years of service}$ $[\frac{1}{2} \times 18,000 \times 38]$	3,42,000	
(iii) Maximum Limit	10,00,000	3,42,000
Taxable Gratuity		58,000

Note: Salary = 10 months average salary preceeding the month of retirement.

= Basic Pay + Dearness Allowance considered for retirement benefits + commission
(if received as a fixed percentage on turnover)

In this case, Average salary for 10 months preceeding the month of retirement is ₹ 18,000 only.



PENSION

Illustration 10. Mr. King is getting a salary of ₹5,400 pm since 1.1.10 and dearness allowance of ₹3,500 pm, 50% of which is a part of retirement benefits. He retires on 30th November 2011 after 30 years and 11 months of service. His pension is fixed at ₹ 3,800 pm. On 1st February 2012 he gets 3/4ths of the pension commuted at ₹1,59,000. Compute his gross salary for the previous year 2011-12 in the following cases:

- If he is a government employee, getting gratuity of ₹ 1,90,000
- If he is an employee of a private company, getting gratuity of ₹ 1,90,000
- If he is an employee of a private company but gets no gratuity.

Solution :

Previous Year 2011-12. Tenure of Service: 1.4.11 to 30.11.11 = 8 months

Post-retirement period: December '11 to March '12 = 4 months

Particulars	Case (i)	Case (ii)	Case (iii)
Salary	43,200	43,200	43,200
D.A	28,000	28,000	28,000
Taxable Gratuity	Exempted	82,750	Nil
Uncommuted Pension [(3,800×2)+(950×2)]	9,500	9,500	9,500
Commuted Value of Pension	Exempted	88,333	
Gross Salary			

Case (ii) Gratuity received by an employee of a private company

		₹
Actual amount received		1,90,000
Less: Exempted amount(least of the followings):		
(i) Actual amount received	1,90,000	
(ii) $\frac{1}{2} \times \text{Avg. Salary} \times \text{No. of years of Completed service}$ [$\frac{1}{2} \times 7,150 \times 30$]	1,07,250	
(iii) Maximum Limit	10,00,000	1,07,250
Taxable Gratuity		<u>82,750</u>
Commuted Value of Pension		
(Non-govt employee, gratuity received)		
Actual commuted value of pension received	1,59,000	
Less: Exempted u/s 10(10A)		
$\frac{1}{3}$ rd of Full Value of Commuted Pension [$\frac{1}{3} \times 2,12,000$]	<u>70,667</u>	
Full Value of Commuted Pension		
$\frac{\text{Amount received on commutation}}{\text{Percentage of pension commuted}} = \frac{1,59,000}{75\%} = 2,12,000$		
Taxable Commuted Value of Pension		<u>88,333</u>

Case(iii) Commuted Value of Pension (Non-govt employee, gratuity not received)

Actual commuted value of pension received	1,59,000	
Less: Exempted u/s 10(10A)		
$\frac{1}{2}$ of Full Value of Commuted Pension [$\frac{1}{2} \times 2,12,000$]	<u>1,06,000</u>	
Full Value of Commuted Pension		
$\frac{\text{Amount received on commutation}}{\text{Percentage of pension commuted}} = \frac{1,59,000}{75\%} = 2,12,000$		
Taxable Commuted Value of Pension		<u>53,000</u>

LEAVE ENCASHMENT

Illustration 11. Mrs. Vandana retires on 16th October 2010 after 30 years and 8 months of service. Salary structure is given below:

FY 2011-12	Salary ₹ 15,000 pm	D.A ₹ 7,500 pm
FY 2010-11	Salary ₹ 12,000 pm	D.A ₹ 6,000 pm

40% of dearness allowance forms a part of superannuation benefits. Record of Earned Leave is given below:
 Leave allowed for one year of completed service -20 days; Leave taken while in service-150 days; Leave encashed during the year-60 days.

Determine the gross salary in the following cases:

- (i) He retires from government service
- (ii) He retires from the service of Delhi Municipal Corporation
- (iii) He retires from the service of Life Insurance Corporation of India
- (iv) He retires from private sector

Solution :

Particulars	Case(i)	Case(ii)	Case(iii)	Case(iv)
Salary for 6 months & 16 days	98,000	98,000	98,000	98,000
Dearness Allowance	49,000	49,000	49,000	49,000
Taxable amount of Leave encashment	Exempted	1,24,980	1,24,980	1,24,980
Gross Income from Salary	1,47,000	2,71,980	2,71,980	2,71,980

Working Notes :

Average monthly salary for 10 months, prior to retirement:	₹
Salary of 6 months 16 days: (1 st April 2011 to 16 th October 2011)	= 98,000
Salary of 3 months 14 days: (14 th December 2010 to 31 st March 2011)	= 41,600
Total Basic Salary	1,39,600
Add: Dearness allowance	
For 6 months 16 days: (1 st April 2011 to 16 th October 2011)	= 49,000
For 3 months 14 days: (14 th December 2010 to 31 st March 2011)	= 20,800
Total D.A.	69,800
D.A. [40% of 69,800, forming part of retirement benefits]	27,920
Total salary of 10 months	1,67,520
Average Salary = 1,67,520 / 10 = 16,752	

Computation of Taxable Leave Encashment :

Amount of encashment received:		
$(30 \times 20) - (150 + 60) \times (15,000 + 7,500) / 30 =$		2,92,500
Less: Exempted u/s 10(10AA) [Least of the followings]		
(i) Actual amount received	2,92,500	
(ii) 10 months salary (preceeding the month of retirement)	1,67,520	
(iii) Leave credit on the date of retirement		
$[(30 \times 20) - (150 + 60) \times (16,752 / 30)]$	2,17,776	
(iv) Maximum Limit	3,00,000	1,67,520
Taxable amount of Leave encashment		1,24,980



Illustration 12. Ms. Parineeta retired from service after 28 years from ABC Ltd. Leave sanctioned by employer 45 days p.a. Leave availed during service 400 days. Leave encashment received: ₹ 4,30,000. Average salary for 10 months preceeding the month of retirement ₹15,000. Compute taxable amount of Leave encashment for the Previous year 2011-12.

Solution :

Since leave sanctioned by the employer is more than 30 days p.a., the following calculation is required, to determine the amount of leave credit on the date of retirement.

Particulars	₹
(i) Leave credit available on the date of retirement = Total Leave sanctioned during tenure of employment – Total leave availed during service = [(28 × 45) – 400]	860
Less: Excess leave sanctioned by the employer [(45– 30 days) per year × 28]	420
Leave credit on the basis of 30 days credit for completed years of service	440
(ii) Leave salary on the basis of 30 days credit = Step (i) × Average Salary = 440 × (15,000/30)	2,20,000

Taxable Leave Salary on Retirement

Particulars	₹	₹
Amount Received on Leave Encashment		4,30,000
Less: Exemption u/s 10(10AA) Least of the followings:		
(i) Actual amount of Leave encashment received	4,30,000	
(ii) Average salary of the individual for the past 10 months × 10 months	1,50,000	
(iii) Maximum Limit	3,00,000	
(iv) Leave at credit at the rate of 30 days p.a. for every Completed year of service as calculated in Step (ii)	2,2,000	1,50,000
Taxable Leave Encashment		2,80,000

RETRENCHMENT COMPENSATION

Illustration 13. Mr. Clever was retrenched from service of UGLY Ltd. The scheme of retrenchment is approved by the Central Government. Retrenchment compensation received ₹8 lakhs. What is the taxability?

Solution : When retrenchment compensation is received in accordance with any scheme, which is approved by the Central Government, it is fully exempted from tax.

Illustration 14. Mr. Flemming was retrenched from service of “GO SLOW Ltd”. Retrenchment compensation received ₹6,00,000. Amount determined under the Industrial Disputes Act, 1948 ₹4,75,000. What is the taxability?

Solution :

Computation of Taxable Retrenchment Compensation

Particulars	₹	₹
Amount received as Retrenchment Compensation		6,00,000
Less: Exemption u/s 10(10B): Least of the followings:		
(i) Actual amount received	6,00,000	
(ii) Amount determined under the Industrial Disputes Act, 1948	4,75,000	
(iii) Maximum Limit	5,00,000	4,75,000
Taxable Retrenchment Compensation		1,25,000

VOLUNTARY RETIREMENT COMPENSATION

Illustration 15. Mr.Hitesh, after serving Z Ltd. for 23 years 7 months, opted the Voluntary Retirement Scheme. Total tenure of service:30 years Compensation received ₹ 8,00,000. Last drawn Salary (i.e. Basic pay + D.A, forming part of retirement benefits) ₹ 15,000.

Compute exemption & taxable value of VRS compensation.

Solution :

Computation of Exemption:

Total tenure of service = $30 \times 12 = 360$ months

Actual length of service = 23 years 7 months = 283 months

No.of months of service left= $(360 - 283)$ months = 77 months

Taxable VRS compensation

Particulars	₹	₹
Amount received as VRS Compensation		8,00,000
Less: Exemption u/s 10(10C): Least of the followings:		
(i) Actual amount received	8,00,000	
(ii) Maximum Limit	5,00,000	
(iii) The highest of the following:		
Last drawn salary $\times 3 \times$ No.of fully completed years of service		
= $15,000 \times 3 \times 23 = 10,35,000$		
• Last drawn salary \times Balance of no.of months of service left.		
= $15,000 \times 77$ months= 11,55,000	11,55,000	5,00,000
Taxable VRS Compensation		3,00,000

DEDUCTIONS AGAINST SALARY

Illustration 16. Ms.Neha is a Senior Accountant in the Ministry of Defence,Govt. of India. She received entertainment allowance ₹5,000 p.m. Her basic salary is ₹35,000 p.m. Professional tax paid ₹5,000. Compute Income from Salary.

Solution :

Computation of Income from Salary

	₹
Basic Salary : $35,000 \times 12$	= 4,20,000
Entertainment Allowance: $5,000 \times 12$	= 60,000
Gross Income from Salary	4,80,000
Less: Deduction u/s 16(ii): Entertainment allowance:	
Least of the following will be allowed as a deduction:	
(i) Actual amount of entertainment allowance received	60,000
(ii) 20% of Basic salary of the Individual [20% of 4,20,000]	84,000
(iii) Statutory limit:	5,000
Exempted amount being the least	5,000
Less: Professional Tax paid u/s 16(iii)	5,000
Income from Salary	4,70,000



VALUATION OF PERQUISITE FOR MEDICAL TREATMENT

Illustration 17. Calculate the perquisite value of the expenditure on medical treatment, which is assessable in the hands of an employee of a company, inclusive of the conditions to be satisfied:

Gross total income, inclusive of salary ₹2,00,000

- (a) amount spent on treatment of the employee's wife in a hospital maintained by the employer ₹20,000
- (b) amount paid by the employer on treatment of the employee's child in a hospital ₹14,000
- (c) medical insurance premium reimbursed by the employer on a policy covering the employee, his wife and dependent parents ₹7,000
- (d) (i) amount spent on medical treatment of the employee outside India ₹2,50,000
(ii) amount spent on travel and stay abroad ₹90,000
- (e) amount spent on travel and stay abroad of attendant ₹60,000

Solution :

Nature of Perquisites	Amount Taxable	Taxability/Non-taxability
Treatment of employee's wife in a hospital	Nil	Fully exempted
Maintained by employers Reimbursement of expenses incurred on treatment of employee's child in hospital	Nil	Not taxable: since the amount is less than ₹ 15,000
Reimbursement of medical insurance premium paid	Nil	Not taxable: since medical insurance premium referred to u/s 80D is paid on the employee and members of his family
Medical treatment outside India	Nil	It is assumed that the whole of such expenditure is permitted by RBI
Amount spent on travel and stay abroad for the employee (herein referred as the patient)	Nil	Not taxable: as the Gross total income does not exceed ₹ 2,00,000
Amount spent on travel and stay abroad of the attendant	Nil	Not taxable: as the Gross total income does not exceed ₹ 2,00,000

PERQUISITE VALUATION OF ACCOMMODATION FACILITIES

Illustration 18. Mr. Goutam is a Central Govt. employee. He is provided with an accommodation. The Licence fee determined by the Government is ₹500 p.m. An amount of ₹50 is deducted from his salary towards such rent. Determine the taxable value of perquisite.

Solution :

Taxable Value of Unfurnished Accommodation: Explanation 1 to Sec.17(2) Rule 3(1)

Licence fee determined by the Government (500×12)	=	6,000
Less: Rent recovered from employee (50×12)	=	600
Taxable value of perquisite	=	5,400

Illustration 19. R submits the following information regarding his salary income for the year 2011-12: Basic salary ₹ 15,000 p.m.; D.A (forming part of salary) 40% of basic salary; City Compensatory Allowance ₹ 300 p.m.; Children Education Allowance ₹ 400 pm per child for 3 children; Transport Allowance ₹ 1,000 p.m. He is provided with a rent free unfurnished accommodation which is owned by the employer. The fair rental value of the house is ₹ 24,000 p.a. Compute the gross salary assuming accommodation is provided in a city where population is (a) exceeding 25 lakhs (b) exceeding 10 lakhs but not exceeding 25 lakhs (c) less than 10 lakhs

Solution :

Computation of Income from Salary

Particulars	Amount	Amount
Basic salary $15,000 \times 12$		1,80,000
D.A. (40% of 1,80,000)		72,000
City Compensatory Allowance (fully taxable) (300×12)		3,600
Children Education Allowance		
Actual amount received $(400 \times 12 \times 3)$	14,400	
Less: Exemption u/s 10(14)		
@ ₹100 per month per child subject to a maximum of 2 children $(100 \times 12 \times 2)$	2,400	12,000
Transport Allowance	12,000	
Actual amount received $(1,000 \times 12)$	9,600	2,400
Less: Exemption u/s 10(14) @ ₹800 p.m. (800×12)		
Gross Income from Salary u/s 17(1)		2,70,000
Add: Value of Unfurnished accommodation u/s 17(2) rule 3(1) explanation 1 Case (a) Population exceeding 25 lakhs 15% of salary Salary = Basic pay + DA(forming part of retirement benefits) + all other taxable allowances = $1,80,000 + 72,000 + 3,600 + 12,000 + 2,400$ = 2,70,000		40,500
Total Income from Salary		3,10,500

Note: Case (b): Where population is exceeding 10 lakhs but not exceeding 25 lakhs

10% of Salary shall be considered as the value of taxable perquisite

$$= 10\% \text{ of } ₹2,70,000 = ₹27,000$$

Case (c) : Where population is less than 10 lakhs

7.5 % of salary shall be considered as the value of taxable perquisite

$$= 7.5\% \text{ of } ₹2,70,000 = ₹20,250$$

Illustration 20. Mr. Kushal submits the following information regarding his salary income which he gets from ABC Ltd. Basic salary ₹15,000 pm; D.A. 40% of basic salary(forming part of retirement benefits);City Compensatory Allowance ₹300pm; Children Education Allowance ₹400pm(for 3 children); Transport allowance ₹1,000 p.m.; Reimbursement of Medical Expenses ₹25,000. He is also entitled to HRA of ₹6,000 p.m. from 1.4.2011 to 31.8.2011. He was paying a rent of ₹7,000 p.m. for a house in Delhi. From 1.9.2011 he was provided with an accommodation by the company for which the company was paying the rent of ₹ 5,000 pm. The company charged him ₹1,000 pm as rent for the accommodation. Compute gross salary for the assessment year 2012-13.

Solution :

Computation of Income from Salary

Particulars	Amount	Amount
Basic salary $15,000 \times 12$		1,80,000
D.A. (40% of 1,80,000)		72,000
City Compensatory Allowance (fully taxable) (300×12)		3,600
House Rent Allowance (April to August 2010)		
Actual amount received $(6,000 \times 5)$	30,000	
Less: Exemption u/s 10(13A) Rule 2A		
Least of the followings:		
(a) Actual amount received	30,000	
(b) 50% of salary	52,500	
(c) Rent paid – 10% of Salary		
$[7,000 \times 5 - 10\% \text{ of } 1,05,000]$	24,500	5,500
Note: Salary for HRA (5 months)		
Basic salary : $15,000 \times 5 =$	75,000	
D.A. = 40% of 75,000 =	30,000	
Total	1,05,000	
Children Education Allowance		
Actual amount received $(400 \times 12 \times 3)$	14,400	
Less: Exemption u/s 10(14)		
@ ₹100 per month per child subject to a maximum of 2 children	2,400	12,000
$(100 \times 12 \times 2)$		
Transport Allowance		
Actual amount received $(1,000 \times 12)$	12,000	
Less: Exemption u/s 10(14) @ ₹ 800 p.m. (800×12)	9,600	2,400
Gross Income from Salary u/s 17(1)		2,75,500
Add: Value of Unfurnished accommodation u/s 17(2) rule		
3(1) Explanation 1		
Assuming Population exceeding 25 lakhs (as accommodation provided in a Metro city)		
15% of salary for 7 months (September 2009 to March 2010)		
Salary = Basic pay + DA (forming part of retirement benefits) + all other taxable allowances		
$= [(15,000 \times 7) + (40\% \text{ of } 1,05,000) + (300 \times 9) + \{(400 \times 9 \times 3) - (100 \times 9 \times 2)\} + \{(1000 - 800) \times 9\}]$		
$= 1,60,500$		24,075
Total Income from Salary		2,99,575

Illustration 21. Mr.Sambhu was provided an accommodation in a hotel by his employer for 22 days before providing him a rent free accommodation which is owned by the employer. The hotel charges paid ₹6,000. Salary for the purpose of accommodation for the period of 22 days is ₹11,000. Compute the taxable perquisite of accommodation.

Solution :

In case of accommodation provided to the assessee on account of transfer, which is exceeding 15 days cumulatively, such shall be taxable as a perquisite. The company recovered ₹1,000 from the employee. Compute taxability.

Lower of the following:

- (i) 24% of salary paid/payable= 24% of 11,000 = 2,640
- (ii) Actual charges paid/payable = 6,000

Less Amount paid or payable by the employee 1,000
Taxable value of perquisite 1,640

Illustration 22. Value of unfurnished accommodation (computed) ₹50,000. Cost of furniture provided by the employer ₹ 80,000. Hire charges of furniture provided in the accommodation ₹500 p.m. Amount recovered from employee ₹200 p.m. Compute taxable value of perquisite.

Solution : Value of Furnished Accomodation (provided at Concessional rates)

Particulars	₹
Value of unfurnished accommodation as above	50,000
Add: Value of Furniture provided:	
• 10%p.a. of original cost of such furniture	8,000
• If hired from third party, then Actual hire charges	6,000
Less: Any charges paid or payable by the employee (200 × 12)	(2,400)
Value of Furnished Accomodation	61,600

Illustration 23. Mr.Ritesh is provided with an accommodation in Kolkata since April 2011. Salary ₹ 40,000 p.m. Cost of furniture provided ₹80,000. On 1st September, 2011, following a promotion with a increase in Salary by ₹15,000, he was transferred to Jharkhand (population less than 25 lakhs but more than 10 lakhs),and was also provided an accommodation there. Mr.Ritesh was allowed to retain the Kolkata accommodation till March, 2012. Compute taxable value of perquisite.

Solution :

Phase 1: Value of Furnished Accommodation (Kolkata) (April to September 2011)

Particulars	₹
Value of unfurnished accommodation (15% of 40,000 × 6 months)	36,000
Add: Value of Furniture provided:	
• 10%p.a. of original cost of such furniture (10% of 80,000 × 6 months)	8,000
Value of Furnished Accommodation	44,000

Phase 2: Valuation of accommodation (October 2011 to December 2011)

- (a) For the first 90 days of transfer: Where accommodation is provided both at existing place of work and in new place, the accommodation, which has lower value, shall be taxable.
- (b) After 90 days: Both accommodations shall be taxable.

Computation for the first 90 days of transfer : (October 2011 to December 2011)

Lower of :

- (i) Value of accommodation at existing place of work
- (ii) Value of accommodation at new place

Value of accommodation at existing place of work (Kolkata)

15% of salary for 3 months (i.e. 90 days) = 15% of 55,000 × 3 months = 24,750

Add: Cost of furniture provided: 10% of 80,000 × 3 months = 24,000

Total Value of Perquisite 48,750



Value of accommodation at new work place (Jharkhand)

10% of salary for 3 months (i.e. 90 days) = 10% of 55,000 × 3 months = 16,500

Therefore, the assessee shall be assessed to tax on ₹ 16,500 (being the lower)

Phase 3: Valuation of accommodation (after 90 days) (January 2012 to March 2012)

For Kolkata accommodation: 15% of 55,000 × 3 months = ₹24,750

Add: Cost of furniture provided: 10% × 80,000 × 3 months = ₹24,000

Total value of perquisite ₹48,750

For Jharkhand accommodation: 10% of 55,000 × 3 months = ₹16,500

Total value of perquisite :

Particulars	Taxable value of perquisite
Phase 1: Accommodation in Kolkata	44,000
Phase 2: Accommodation in Jharkhand (being the lower during 90 days)	16,500
Phase 3: Accommodation in Kolkata	48,750
	16,500
Total Value of Taxable Perquisite	1,25,750

OTHER FACILITIES AND PERQUISITES TO EMPLOYEE AND HIS HOUSEHOLD

Illustration 24. Mr.E is employed with N Ltd. he also gets the services of sweeper and watchman. Determine his gross salary in the following cases:

- 1) His salary is ₹ 4,200 pm. Employer provides the services of sweeper and watchman. He pays them ₹ 600 pm and ₹ 500 pm;
- 2) His salary is ₹ 4,200 pm. Sweeper and watchman are engaged by N at the rates given in clause(1) above but their wages are reimbursed by the employer;
- 3) His salary is ₹ 4,210 pm. Employer provides the services of sweeper and watchman at the above rates but he recovers from N ₹ 200 pm and ₹ 300 pm respectively.

E has paid employment tax of ₹ 400.

Solution :

Particulars	Case (1)	Case (2) [Ref.Sec.17(2)(iv), Rule 3(3)]	Case (3) [Ref.Sec.17(2)(iii) Rule 3(3)]
Salary	50,400	50,400	50,520
Wages of sweeper	Sec.17(2)(iii) not taxable	7,200	4,800
Wages of watchman	Sec.17(2)(iii) not taxable	6,000	2,400
Gross salary	50,400	63,600	57,720

Working Note :

Case (1): He is a non-specified employee. Perquisites provided by employer u/s 17(2)(iii) are not chargeable to tax:

Salary: 4,200 × 12 = 50,400

Less: Professional tax paid u/s 16(iii) = 400

Monetary income not exceeding ₹ 50,000 = 50,000

Case (2): If the facility is engaged by the employee but reimbursed by the employer, it is an obligation of employee, discharged by employer u/s 17(2)(iv), it is always taxable.

Case (3): He is a specified employee, as his monetary income, chargeable under the head “salaries” exceeds ₹ 50,000.

Gross salary; $4,210 \times 12$	= 50,520
Less: Professional tax paid u/s 16(iii)	= 400
Monetary income exceeding ₹ 50,000	₹ 50,120

Illustration 25. G Ltd. provides electricity to its employee, P. Annual consumption as per meter reading comes to 2,250 units. Determine the value of the perquisite in the following cases:

- 1) Electricity meter is in the name of P and the rate of electricity is ₹3 per unit
- 2) Electricity meter is in the name of G Ltd. the rate of electricity is ₹3 per unit.
- 3) G Ltd. is a power-generating company. Manufacturing cost is 90 paise per unit but supplied to public @ ₹2 per unit. However, it charges 30 paise per unit from employees.

Solution: With reference to Rule 3(4)

- 1) Perquisite value of free electricity is ₹6,750 ($2,250 \times 3$). As the electric meter is in the name of the employee, it is his obligation to pay the bill. However, as the bill has been paid by the employer, it is an obligation of employee, discharged by the employer. It is always taxable u/s 17(2)(iv).
- 2) Perquisite value of free electricity will be ₹6,750. It shall be assessed to tax, if the employee is a specified employee as per Sec.17(2)(iii)
- 3) Perquisite value of electricity supplied = $2,250 (0.90 - 0.30) = ₹ 1,350$

Illustration 26. Determine the value of education facility in the following cases:

- 1) Three children of G, an employee of S Ltd., are studying in a school, run by S Ltd. School fees is ₹2,500 pm and hostel fees is ₹2,000 pm. But the employer recovers only ₹600 pm and ₹500 pm respectively. However, a similar school or a hostel around the locality charges ₹1,800 pm and ₹1,200 pm respectively.
- 2) The employer has also reimbursed the school fees of ₹1,200 pm of his nephew, fully dependent on him after the death of his brother.

Solution :

Computation of taxable value of education facility [As per Rule 3(5)]

Particulars	Taxable value of perquisite
1. (a) School fees of his children, studying in a school run by employer : (₹1,800 × 3 × 12) – (1,000 × 3 × 12) – (600 × 3 × 12)	7,200
(b) Hostel fees: (2,000 × 3 × 12) – (500 × 3 × 12)	54,000
2. School fee of nephew (1,200 × 12)	14,400
Total value of taxable perquisite	75,600

Illustration 27. Mr. Z is the manager of F Ltd. his son is a student of Amity International School. School fees of ₹ 4,000 pm and hostel fees of ₹ 3,000 pm., are directly paid by Z Ltd. to the school but it recovers from Z only 30%. F also joins an advanced course of Marketing Management for 4 months at IIM, Ahmedabad, fees of the course, ₹ 2,50,000 is paid by F Ltd. Determine the perquisite value of the education facility.



Solution :

Computation of taxable value of education facility [As per Rule 3(5)]

Particulars	Taxable value of perquisite (₹)
(1)(a) School fees of his children, studying in a school run by employer: (₹4,000 × 12) - (1,200 × 12)	33,600
(b) Hostel fees: (3,000 × 12) – (900 × 12)	25,200
2) Fees paid for Marketing Management course for Mr.Z (it is a fully exempted perquisite)	Nil
Total value of taxable perquisite	58,800

Illustration 28. Mr.D takes interest-free loan of ₹ 2,50,000 on 1.11.11 from his employer to construct his house. The loan is repayable in 50 monthly installments from January 2011. Compute the value of interest free loan. SBI Lending rate 8.5% p.a. (for housing loans not exceeding 5 years).

Solution :

Computation of taxable value of Loan provided by employer [As per Rule 3(7)(i)]

Time period during which loan remains outstanding	Balance on the last day of the month
November	2,50,000
December	2,50,000
January	2,45,000
February	2,40,000
March	2,35,000
Total	12,20,000
Perquisite value of interest-free loan : $12,20,000 \times 8.5\% \times 1/12 = ₹ 8,642$	

Illustration 29. Mr.Prabir Nandy is a Manager in H Ltd. He gets salary @ ₹ 30,000 pm. He is also allowed free use of computer, video-camera and television of the company. H Ltd. has purchased (i) Computer for ₹ 1,00,000 (ii) Video-camera for ₹ 30,000. Their written down value on 1.4.09 is ₹ 60,000 and ₹ 30,000 respectively. Television set has been taken on lease rent @ ₹ 100 pm. The employer recovers ₹ 500 per month for use of the assets. Compute his gross salary for the assessment year 2012-13.

Solution :

Computation of taxable value of Loan provided by employer [As per Rule 3(7)(vii)]

Salary : 30,000 × 12	3,60,000
Add: Free use of computer, u/s 17(2)(vi) read with Rule 3(7)(vii)	Nil
Add: Free use of video camera, u/s 17(2)(vi) read with rule 3(7) (vii) [10% of 30,000]	3,000
Add: Free use of telephone, u/s 17(2)(vi) read with rule 3(7)(vii) (100 × 12)	1,200
Gross Salary	3,64,200

Illustration 30. Mr.C is an accountant of D Ltd. He gets salary of ₹25,000 pm. He has purchased motor car and washing machine from the company on 1 February 2011. Particulars of cost and sale price of the two assets are given below :

Year of Purchase	Particulars of the Asset	Purchase Price (Rs)	Sale price (Rs)
01.07.2008	Motor car	2,50,000	85,000
15.09.2007	Washing Machine	10,000	5,000

Compute the taxable value of perquisites for the assessment year 2012-13.

Solution :

Computation of taxable value of perquisites on transfer of moveable assets

[As per Rule 3(7)(viii)]

TRANSFER OF MOVABLE ASSET TO EMPLOYEES

Nature of Assets transferred	Amount
Motor car (Actual Cost)	2,50,000
Less: Depreciation @ 20% on WDV from 01.07.2008 to 30.06.2009	50,000
WDV	2,00,000
Less: Depreciation @ 20% on WDV from 01.07.2009 to 30.06.2010	40,000
WDV	1,60,000
Less: Depreciation @ 20% on WDV from 01.07.2010 to 30.06.2011	32,000
WDV	<u>1,28,000</u>
Washing Machine (Actual Cost)	10,000
Less: Depreciation @ 10% on SLM from 15.09.2007 to 14.09.2008	1,000
WDV	9,000
Less: Depreciation @ 10% on WDV from 15.09.2008 to 14.09.2009	1,000
WDV	8,000
Less: Depreciation @ 10% on WDV from 15.09.2009 to 14.09.2010	1,000
WDV	7,000
Less: Depreciation @ 10% on WDV from 15.09.2010 to 14.09.2011	1,000
WDV	<u>6,000</u>

Particulars	Motor Car	Washing Machine
WDV on the Asset	1,28,000	6,000
Less: Amount recovered from employee	85,000	5,000
Taxable value of perquisite	43,000	1,000



Illustration 31. Shri A. Chakraborty, Director (Administration) in MNPC Ltd. He is entitled to a motor car (1.8 ltrs.) to be used for both official & private purposes.

Discuss the taxability of perquisite if :

- (i) The car is owned by the employer, expenses paid by employer & it is a chauffeur driven car.
- (ii) The car is owned by Sri Chakraborty. Expenses incurred ₹ 20,000 & chauffeur paid a salary of ₹ 60,000 provided by the employer.

Solution :

As per notification No. 24 dated 18.12.09, the taxable value of perquisite will be :

$$\begin{aligned} \text{(i) } ₹ 2,400 \text{ p.m} + ₹ 900 \text{ p.m for chauffeur} &= ₹ 3,300 \text{ p.m} \times 12 \text{ months} \\ &= ₹ 39,600 \end{aligned}$$

(ii) Value of Perquisite	₹
Amount of expenses	20,000
(+) Salary to chauffeur	60,000
	80,000

<i>Less :</i> Value of Perquisite if the car was owned by the employer [as computed in (i) above]	39,600
	<u><u>40,400</u></u>

Illustration 32. Aniket joined a company on 1.7.2011 and was paid the following emoluments and allowed perquisites as under :

Emoluments : Basic Pay ₹ 35,000 per month; D.A. ₹ 20,000 per month; Bonus ₹ 20,000 per month.

Perquisites :

- (i) Furnished accommodation owned by the employer and provided free of cost;
- (ii) Value of furniture therein ₹ 3,60,000; Hire charges of Furniture provided ₹ 20,000 p.a.
- (iii) Motor car owned by the company (with engine c.c. less than 1.6 litres) along with chauffeur for official and personal use, expenses met by Employer.
- (iv) Sweeper salary paid by company ₹ 1,500 per month; amount recovered @ ₹ 200 pm.
- (v) Watchman salary paid by company ₹ 1,500 per month; amount recovered @ ₹ 300 pm.
- (vi) Educational facility for 2 children provided free of cost. The school is owned and maintained by the company. Elder child studies in class V and younger child in class II. Tuition fee per month ₹ 1,600 & ₹ 900 respectively.
- (vii) Loan of ₹ 5,00,000 repayable within 7 years given on 1.10.2011 for purchase of a house. No repayment was made during the year; let charged by employer @ 2% p.a. Interest chargeable as per Income Tax Act @ 10% p.a.
- (viii) Interest free loan for purchase of computer ₹ 50,000 given on 1.2.2012. No repayment was made during the year;
- (ix) Corporate membership of a club. The initial fee of ₹ 1,00,000 was paid by the company. Aniket paid the bills for his use of club facilities.

You are required to compute the income of Aniket under the head “Salaries” in respect of assessment year 2012-13.

Solution :

Assessee : Mr. Aniket

A.Y. 2012-13

Computation of Income under the head ‘Salaries’

(i)	Basic Pay	(35,000 × 9)	3,15,000
(ii)	D.A.	(20,000 × 9)	1,80,000
(iii)	Bonus	(20,000 × 9)	1,80,000
(iv)	Value of furnished accommodation	Note 1	1,28,250
(v)	Motor car	(1,800+900) × 9 m	24,300
(vi)	Sweeper Salary	(1,500–200) × 9 m	11,700
(vii)	Watchman Salary	(1,500–300) × 9 m	10,800
(viii)	Education facility	Note 2	5,400
(ix)	Interest free housing loan	Note 3	23,333
(x)	Interest free computer loan	Note 4	1,375
(xi)	Corporate membership fee		1,00,000
	Gross Salary		8,80,158
	Taxable Salary		8,80,158

Value of Furnished Accommodation

Note 1.

Particulars		Amount
Salary for this purpose -		
Basic Salary	(35,000 × 9)	3,15,000
D.A	(20,000 × 9)	1,80,000
Bonus	(20,000 × 9)	1,80,000
Total		6,75,000



Assuming, Mr. Ankit stays in a city where population is more than 25,00,000 as per 2001 census,

Value of unfurnished accommodation	= 15% of salary
	= 15% of 6,75,000
	= ₹ 1,01,250
Value of furniture provided	= 10% p.a. of actual cost
	= 10% of 3,60,000 × 9/12
	= ₹ 27,000

(Assuming, value of furniture given in the problem represents actual cost.)

Value of rent free furnished accommodation	= 1,01,250 (+) 27,000
	= ₹ 1,28,250

Assumption: DA is included as a part of retirement benefits.

Note 2.

Value of Educational Facility

Where the school is owned and maintained by employer, if the cost of education provided is less than ₹ 1,000 p.m. then the value of perquisite is NIL. If the cost of education exceeds ₹ 1,000 p.m. then the value of perquisite will be equal to the actual cost of education provided in excess of ₹ 1,000 p.m. per child maximum for two children.

Value of perquisite for elder child = ₹ (16,000 – 1,000) × 9 m = 5,400

Value of perquisite for younger child = NIL, since tuition fee per month is less than ₹ 1,000.

Assuming, cost of education provided to Babu's children is less than ₹ 1,000 p.m. value of perquisite provided is NIL.

Note 3.

Interest free housing loan

Value of perquisite	= Interest @ 10% p.a. less Actual interest charged
	= (10% – 2%) × 5,00,000 × 7/12 = ₹ 23,333.

Note 4.

Interest free computer loan

Value of perquisite	= Interest @ 16.50% p.a. less Actual interest charged
	= (16.50% – 0%) × 50,000 × 2/12 = ₹ 1,375.

Illustration 33. A was employed with Z Ltd. He retired w.e.f. 1.2.2012 after completing a service of 24 years and 5 months. He submits the following information :

Basic Salary	₹ 5,000 per month (at the time of retirement)
Dearness Allowance	100% of Basic Salary (60% of which forms part of salary for retirement benefits).
Last increment	₹ 500 w.e.f. 1.7.2011

His pension was determined at ₹ 3,000 per month. He got 50% of the pension commuted w.e.f. 1.3.2011 and received a sum of ₹ 1,20,000 as commuted pension. In addition to this, he received a gratuity of ₹ 1,50,000 and leave encashment amounting to ₹ 56,000 on account of accumulated leave of 240 days. He was entitled to 40 days leave for every year of service.

Compute his Gross Salary for assessment year 2012-13 assuming that he is not covered under Payment of Gratuity Act.

Solution :

Computation of Gross Salary for the Assessment Year 2012-13

Particulars	₹	₹
Basic Pay : April '11 to June '11 = 3 months @ ₹ 4,500 pm	13,500	
July 11 to June '12 = 7 months @ ₹ 5,000 pm	35,000	48,500
Dearness Allowance @ 100% of Basic Pay		48,500
Uncommuted Pension		
February @ ₹ 3,000 pm	3,000	
March @ ₹ 1,500 pm	1,500	4,500
(Since 50% commuted)		
Commuted Value of Pension		
Amount Received	1,20,000	
Less : Exemption u/s 10(10A)		
1/3 of Value of Commuted Pension $\left(\frac{1}{3} \times 2,40,000\right)$	80,000	40,000
Full value of Commuted Pension $= \frac{\text{Amount Received}}{\% \text{ Commuted}}$		
$= \frac{1,20,000}{50\%} = 2,40,000$		
Gratuity :		
Amount received	1,50,000	
Less : Exempt (See note No. 1)	93,120	56,880
Leave of the followings :		
(i) Actual Amount Received	1,50,000	
(ii) Maximum limit	10,00,000	
(ii) 1/2 months average salary	93,120	
for each years of completed		
Service $\left(\frac{1}{2} \times 7,760 \times 24\right)$		
Salary for Gratuity (not covered by Payment of Gratuity Act)		
= Basic Pay + D/A (Forming part for retirement benefit)		
Average Salary = $\frac{\text{Total Salary of 10 months preceeding the month of retirement}}{10}$		
$= \frac{48,500 + 50\% \text{ of } 48,500}{10} = \frac{48,500 + 29,100}{10} = 7,760$		

Leave Encashment			
Amount received		56,000	
Less : Exemption u/s 10(10AA)			
Least of the followings :			
(i) Actual Average Salary	56,000		
(ii) 10 months average salary (10×7760)	77,600		
(iii) Maximum limit	3,00,000		
(iv) Leave Credit	NIL	NIL	56,000
as per Note			
Notes :			
Calculation of Leave Credit			
Total leave entitlement (24 yrs × 40 days p.a.)		= 960 days	
Less : Leave Availed during service		720 days	
= Total leave entitlement – Leave encashment			
= (960 – 240)		240 days	
Less : Excess Leave in excess of 30 days p.a.		240 days	
(24 (40 – 30))			
Leave credit		NIL	
Gross Income from Salary			2,54,380

Illustration 34. Vineet had been working with M Ltd., in a tribal area since 1-10-1997. He was entitled to the following emoluments:

1. Basic salary w.e.f. 1-1-2011 ₹ 6,000 p.m.
2. Dearness allowance 50% of basic salary (40% of which forms part of salary for retirement benefits)
3. Medical allowance ₹ 1500 p.m., (entire amount is spent on his own medical treatment).
4. Entertainment allowance ₹ 400 p.m.
5. Children education allowance ₹ 80 p.m. per child for three children.
6. Hostel expenditure allowance ₹ 100 p.m. per child for three children.
7. Uniform allowance ₹ 250 p.m. (He spends ₹ 1,500 on the purchase and maintenance of uniform)
8. House rent allowance ₹ 750 per month. He pays ₹ 1,000 per month as rent.
9. He contributes ₹ 900 per month to a recognised provident fund to which his employer contributes an equal amount.

He resigned from his job on 1.1.2012 and shifted to Delhi. He was entitled to the following benefits at the time of his retirement :

- (a) Gratuity ₹ 1,35,000
- (b) Pension from 1.1.2012 ₹ 3,000 p.m.
- (c) Payment from recognised provident fund ₹ 3,00,000
- (d) Encashment of earned leave for 150 days ₹ 36,000

He was entitled to 40 days leave for every completed year of service. He got 50% of his pension commuted in lumpsum w.e.f. 1.3.2012 and received ₹ 1,20,000 as commuted pension.

He joined K Ltd. at Mumbai w.e.f. 1-2-2012 and was entitled to the following emoluments:

- (1) Basic salary ₹ 5,000 p.m.
- (2) Dearness allowance (forming part of salary) 20% of basic salary

- (3) Rent-free unfurnished accommodation in Delhi which is owned by the employer and whose fair rental value is ₹ 48,000 p.a.

He was also given the following facilities by the employer :

- Motor car (1.4 ltr. engine capacity) with driver, which he uses partly for official and partly for personal purposes.
- The monthly expenses incurred by 'A' on gas and electricity were ₹ 500 which were reimbursed by the employer.
- Reimbursement of educational expenses of his two children which amounted to ₹ 350 p.m.
- On 4.3.2011 his wife fell ill and the employer reimbursed the expenditure of medical treatment amounting to ₹ 17,500.
- A watchman, a sweeper, a cook and a gardener have been provided to whom the company pays a salary of ₹ 400 p.m. each.
- Loan of ₹ 1,00,000 @ 8% p.a. for construction of his house was given by the company. SBI rate of interest is 7% p.a.

He made the following payments during the previous year :

- Professional tax ₹ 500
- LIP on his life policy of ₹ 1,00,000 – ₹ 15,000.
- Deposit in PPF account ₹ 50,000.

Compute his total income and tax liability for the assessment year 2012-13.

Solution :

Assessee : Mr. Vineet

A. Y : 2012-13

Computation of Total Income and Tax Liability

Particulars	₹	₹
Employer – M Ltd.		
Basic salary $6,000 \times 9$		54,000
DA @ 50% of Basic Salary		27,000
Medical allowance @ ₹ 1,500 pm $\times 9$ months		13,500
Entertainment allowance @ ₹ 400 pm $\times 9$ months		3,600
Children education allowance $80 \times 3 \times 9$	2,160	
Less : Exempt u/s 10(14) = $80 \times 2 \times 9$	440	720
Hostel expenditure allowance $100 \times 3 \times 9$	2,700	
Less : Exempt u/s 10(14) = $100 \times 2 \times 9$	1,800	900
Uncommuted pension $(2,000 \times 2 + 1,000 \times 1)$		5,000
Uniform allowance $(250 \times 9 - 1500)$		750
House Rent Allowance		
Amount Received 750×9	6,750	
Less : Exemption u/s 10(13A) Rule 2A		
Lease of the followings :		
(i) Amount Received	6,750	
(ii) 40% of Salary	25,920	
(iii) Rent paid – 10% of Salary	2,520	
$(1000 \times 9 - 6,480)$		4,230

Salary for HRA = Basic Pay + Dearness Allowance (forming part of salary) + Commission (if received at a fixed per centage on turnover) = 54,000 + (40% of 27,000) = 54,000 + 10,800 = 64,800 Employer's Contribution to RPF @ ₹ 900 pm × 9 months Less : Exemption u/s 10(14) upto 12% of salary Salary = Basic Pay + D.A (forming part) = 54,000 + 40% of 27,000 = 64,800 ∴ 12% of 64,800 =	8,100	
Gratuity — (form A Ltd.) Actual Amount Received 1,25,000 Less : Exemption u/s 10(10) Least of the followings : (i) Actual Amount Received 1,25,000 (ii) Max. limit 10,00,000 (iii) 1/2 months average salary for each years of completed service 50,400 [1/2 × 7,200 × 14]	7,776	324
Salary for Gratuity (not covered by Payment of Graguity Act) = Basic Pay + D/A (forming part for retirement benefits) + Commission (if received at a fixed percentage on turnover) Again, Average Salary = Salary for 10 months preceeding the month of retirement B/P = 6,000 × 10 = 60,000 D/A (forming part) = 40% × 50% × 6,000 = 12,000 72,000 ∴ Average Salary per month = $\frac{72,000}{10} = 7,200$	50,400	74,600
Commuted Value of Pension Amount Received 1,20,000 Less : Exemption u/s 10(10A) 1/3 of Full Value of Commuted Pension [$\frac{1}{3} \times 2,40,000$] Full Value of Commuted Pension = $\frac{\text{Amount Received}}{\% \text{ Commuted}}$ = $\frac{1,20,000}{50\%} = 2,40,000$ Payment from RPF (Exempt)	80,000	40,000
		—

Leave encashment – Actual amount	36,000	
Less : Exemption u/s 10(10AA)	4,800	31,200
		2,55,824
List of the followings:		
(a) Actual encashment	₹ 36,000	
(b) Eligible encashment $(7,200/30 \times 20)$	₹ 4,800	
(c) 10 months average salary $(7,200 \times 10)$	₹ 72,000	
(d) Amount specified	₹ 3,00,000	
Leave encashment shall be exempt as under :		
Completed years of service	13 years	
Number of days leave allowed every year	40	
Total leave allowable	520 days	
Leave encashed	150 days	
Therefore leave availed $(520 - 150)$	370 days	
Leave available on basis of 30 days (30×13)	390 days	
Less : Leave availed	370 days	
Therefore encashment eligible for exemption $(390 - 370)$	20 days	
Employer — S Ltd.		
Basic salary $5,000 \times 2$	10,000	
Dearness Allowance @ 20% of B/Pay	2,000	
Motor Car facility $(1,800 + 900) \times 2$ months	5,400	
Free Gas/Electricity (500×2)	1,000	
Education Re-imbursement (350×2)	700	
Medical Re-imbursement $(17,500 - 15,000)$	2,500	
Watchment (400×2)	800	
Sweeper (400×2)	800	
Cook (400×2)	800	
Gardener (400×2)	800	
Interest on Loan (not taxable as interest charged is more than the rate of SBI)	—	
Perquisite for Value of Rent-free unfurnished accommodation	2,250	27,050
Valuation of unfurnished rent-free accommodation :		
15% of salary which includes the following:		
Basic $(5,000 \times 2)$	₹ 10,000	
DA	₹ 2,000	
Uncommuted pension from R Ltd. $(2,000 + 1,000)$	₹ 3,000	
	₹ 15,000	
Value of the unfurnished accommodation 15% of ₹ 15,000 = ₹ 2,250		
Aggregate salary from M Ltd. and S Ltd.		2,82,874
Less : (i) Entertainment allowance u/s 16(ii)	Nil	
(ii) Professional-tax u/s 16(iii)	500	500
Income from salary		2,82,374
Other Income		Nil
Gross Total Income		2,82,374
Less : Deduction u/s 80C		
RPF (900×9)	8,100	
LIP	15,000	
PPF	50,000	73,100
Total Income (rounded off)		2,09,274



Total Income (Rounded of u/s 288)

2,09,270

Tax on ₹ 2,09,270

upto ₹ 1,80,000

= Nil

@ 10% on (209270 – 1,80,000) = 10% of 29270

= 2927

2,927

Add : Education cess @ 2%

58

Add : SHEC @ 1%

29

Total tax liability

3,014

Tax Payable (Rounded off u/s 288A)

= ₹ 3010

Since he has received lump sum payment on account of gratuity, commuted pension and leave encashment, he can claim relief u/s 89 if the same is beneficial to him.

Illustration 35. Ramesh retired as General Manager of XYZ Co. Ltd. on 30.11.2011 after rendering service for 20 years and 10 months. He ₹ 9,00,000 as gratuity from the employer. (He is not covered by Gratuity Act, 1972). His Salary details as below -

Basic Pay	₹ 30,000 p.m. upto 30.06.2011
Basic Pay	₹ 32,000 p.m. from 01.07.2011
Dearnes Allowance (Eligible for Retirement Benefits)	50% of Basic Pay
Transport Allowance	₹ 4,500 p.m.

Ramesh resides in his own house. Interest on monies borrowed for the self-occupied house is ₹ 84,000 for the year 31.3.2012.

From a Fixed Deposit with a Bank, he earned Interest Income of ₹ 18,000 for the year ending 31.3.2012. He also invested ₹ 30,000 in long-term infrastructure Bond and ₹ 80,000 in PPF.

Compute Taxable Income of Ramesh for the year ended 31.03.2012.

Assessee : Mr. Ramesh

Previous Year : 2011-2012

Assessment Year : 2012-13

Computation of Total Income

Particulars	₹	₹	₹
(A) Salaries : Salary from XYZ Co. Ltd			
1. Basic Salary (₹ 30,000 × 3 + ₹ 32,000 × 5)			2,50,000
2. Dearness Allowance (50% of Basic Salary =		1,25,000	
3. Transport Allowance (₹ 4,500 × 8)		36,000	
Less: Exempt u/s 10(14) (₹ 800 × 8 Months)		(6,400)	29,600
4. Gratuity Received (Not covered under Payment of Gratuity Act)		9,00,000	
Less: Exemption u/s 10(10) = Least of the following —			
• Actual Amount received 9,00,000			
• ½ months average salary for each years of completed service = ½ × 30,800 × 20 years	3,08,000		
• Maximum Limit	10,00,000	3,08,000	5,92,000
Average Salary for Gratuity =			
Basic Pay + DA (forming part) for the last 10 months preceeding the moth of retirement			
10			
= $\frac{32,000 \times 4 + 30,000 \times 6}{10} = \frac{3,08,000}{10} = 30,800$			

Gross Salary			9,96,600
Less: Deduction u/s 16			Nil
Income under the head Salary			9,96,600
(B) Income from House Property			
Self Occupied — Annual Value		Nil	
Less : Deduction u/s 24 — Interest on Borrowed Capital		(84,000)	(84,000)
(C) Income from Other Sources : Bank Interest ₹			18,000
(D) Gross Total Income			9,30,600
Less : Deduction under Chapter VIA			
u/s 80C – Deposit in PPF ₹ 80,000			
(Maximum amount allowed as deduction)			70,000
u/s 80 CCF – Subscription to Long-term Infrastructure Bonded			
– Amount deposited ₹ 30,000 remitted upto			20,000
(E) Total Income			8,40,600

Illustration 36. Mr. Ganesh retires on 31.10.2011 voluntarily from XYZ (P) Ltd as per the scheme u/s (10C) of the Income-tax Act, 1961. He furnishes the following particulars :

- | | |
|---|--------------|
| (a) Basic Pay | ₹ 20,000 pm. |
| (b) Pension | ₹ 8,000 pm. |
| (c) D.A. forming part of Salary for retirement benefits | ₹ 6,000 pm. |
| (d) Compensation of voluntary retirement | ₹ 6,00,000 |
| (e) Gratuity | ₹ 1,50,000 |
| (f) Leave Salary | ₹ 40,000 |
| (g) He gets 60% of his pension commuted for ₹ 90,000 on 31.1.2011. Completed years of service 18 years and 7 months. Leave availed while in service 19 months. But for the voluntary retirement, Mr. Ganesh would have retired only after 45 months. The last increment he received was on 1.11.2010. | |

Compute his taxable salary income for the A.Y. 2012-13.

Solution :

Assessee : Mr. Ganesh

Previous Year : 2011-2012

Assessment Year : 2012-13

Computation of Total Income

Particulars		₹
Basic salary	(₹ 20,000 × 7)	1,40,000
Dearness Allowance	(₹ 6,000 × 7)	42,000
Gratuity	(W.N. 1)	NIL
Pension	(W.N.2)	70,400
Voluntary Retirement Compensation	(W.N.3)	1,00,000
Leave Encashment	(W.N.4)	90,000
Income under the head “Salaries”		4,42,400

Working Notes :

(a) Taxable Gratuity

Particulars	₹	₹
Gratuity received (assumed as not covered by Payment of Gratuity Act, 1972)		1,50,000
Less : Exempt u/s 10(10) :		
Least of the following —		
(i) Actual Amount of Gratuity Received	1,50,000	
(ii) Maximum Limit	10,00,000	
(iii) $\frac{1}{2}$ months average salary for each years of completed service ($\frac{1}{2} \times 18 \times 26,000$)	2,34,000	(1,50,000)
Average Salary = $\frac{26,000 \times 10}{10} = 26,000$		
Taxable Gratuity		NIL

(b) Taxable Pension

Particulars	₹	₹
(a) Uncommuted Pension		
• Period: November 2010 - January 2011 (₹ 8,000×3 Months)	24,000	
• Period: February 2011 - March 2011 (₹ 8,000×40%×2 Months)	6,400	
• Total		30,400
(b) Commuted Pension		
Amount Received	90,000	
Less : Exempt u/s 10(10A)		
1/3rd of Full Value of Commuted Pension (Since Gratuity received)		
[1/3rd of (90,000/60) × 100] (Note 1) (50,000)	40,000	
Taxable Pension		70,400

(C) Computation of Taxable VRS Compensation

Particulars	₹	₹
Amount of VRS Compensation Received		6,00,000
Less: Exempt u/s 10(10C):		
Least of the following —		
• Actual Amount Received	6,00,000	
• Maximum Limit	5,00,000	
• The above shall not exceed higher of :		
(i) Last Drawn Salary × 3 × No. of completed years of service (26,000 × 3 × 18 Years)	14,04,000	
(ii) Last drawn Salary × balance of months of service left (26,000 × 45 Months)	5,40,000	(5,00,000)
Taxable Value of VRS Compensation		1,00,000

(D) Computation of Taxable Leave Encashment

Particulars	₹	₹
Amount of Leave Encashment Received		90,000
Less : Exemption u/s 10(10AA) :		
Least of the following :		
(i) Amount Received	90,000	
(ii) Notified Amount	3,00,000	
(iii) Average salary of past 10 months Salary x 10 months (12,000 × 10)	1,20,000	
(iv) Leave Encashment based on 30 days credit for every completed year of service (Note)	Nil	Nil
Taxable Leave Encashment		90,000

Note :

Total Leave Eligible on basis of 30 days credit for every completed years of service of 18 years	18 Months
Total Leave Taken	19 Months
Leave to his credit	Nil

Illustration 37. M Ltd. has sold the following assets to its employee, Mr. Raghu. Compute taxable perquisite.

Assets	Date of purchase	Purchase value	Date of sale	Sale price
Computer	1-7-08	2,00,000	18-8-2011	20,000
Car	1-4-09	3,00,000	1-3-2012	50,000
Television	1-4-06	50,000	1-4-2011	2,000
Sofa set	1-4-96	80,000	1-7-2011	5,000

Solution :

Computation of taxable value of perquisite in hands of Mr. Amit for the A.Y. 2012-13.

Assets	Written down value	Sale value	Taxable perquisite
Computer	25000 (Note 1)	2,000	5,000
Car	192000 (Note 2)	50,000	1,42,000
Television	25000 (Note 3)	2,000	23,000
Sofa set	Nil ⁴	5,000	Nil
Taxable Perquisite		1,70,000	

1. Calculation of WDV of Computer

Particulars	Amount
Purchase value	2,00,000
Less : Depreciation from 1-7-08 to 30-6-09 @ 50%	1,00,000
WDV as on 1-7-09	1,00,000
Less : Depreciation from 1-7-09 to 30-6-10 @ 50%	50,000
WDV as on 1-7-10	50,000
Less : Depreciation from 1-7-10 to 30-6-11 @ 50%	25,000
WDV as on 1-7-11	25,000
Less : Depreciation from 1-7-11 to 18-8-11 (as year not complete)	Nil
WDV as on the date of sale	25,000



2. Calculation of WDV of Car

Particulars	Amount
Purchase value	3,00,000
Less : Depreciation from 1-4-09 to 31-3-10 @ 20%	60,000
WDV as on 1-4-10	2,40,000
Less : Depreciation from 1-4-10 to 31-3-11 @ 20%	48,000
WDV as on 1-4-11	1,92,000
Less : Depreciation from 1-4-11 to 1-3-12 @ (as year not completed)	Nil
WDV as on date of sale	1,92,000

3. Calculation of WDV of Television

Particulars	Amount
Purchase value	50,000
Less : Depreciation from 1-4-06 to 31-3-11 @ 10%	25,000
WDV as on date of sale	25,000

4. Depreciation on sofa set is charged @ 10% as per straight-line method. Since the asset is used for more than 10 years, hence its WDV will be Nil.

Illustration 38. Hema, aged about 66 years is a Finance Manager of Udyog Pvt. Ltd. based at Mumbai. She is in continuous service since 1969 and received the following from the Company during the year 31.3.2012.

- Basic Pay $(50,000 \times 12) = ₹ 6,00,000$
- D.A $(20,000 \times 12) = ₹ 2,40,000$
- Bonus 2 months Basic Pay
- Commission — 0.1% of Company's Turnover. Turnover for financial year 2011-2012 was ₹ 15 Crores.
- Contribution of the Employer and Employee to the PF Account ₹ 3,00,000 each
- Interest credited to P.F Account at 10% ₹ 60,000
- Rent Free Unfurnished Accommodation provided by the Company (Company pays ₹ 70,000 p.a. rent)
- Entertainment Allowance ₹ 30,000
- Children's Education Allowance to meet the hostel expenditure of three children ₹ 5,000 each.

Hema makes the following payments and Investments :

- Premium paid to insure the life of her major son ₹ 15,000
- Medical Insurance Premium for Self — ₹ 15,000, Spouse ₹ 15,000 (Aged 70 yrs.)
- Donation to Public Charitable Institution registered under Section 80G ₹ 2,00,000
- LIC Pension Fund ₹ 12,000
- Long-term Infrastructure Bond — ₹ 25,000

Determine the tax liability for the Assessment Year 2012-13.



Assessee : Mr. Lakshmi

Previous Year: 2011-2012
Computation of Total Income

Assessment Year : 2012-13

Particulars	₹	₹
Basic Salary (₹ 50,000×12)		6,00,000
Dearness Allowance (₹ 20,000×12)		2,40,000
Bonus (₹ 50,000×2)		1,00,000
Commission (₹ 15 Crores×0.1%)		1,50,000
Employer's Contribution to Provident Fund	3,00,000	
Less : Exemption u/s 10(14) upto 12% of Salary (12% × 9,90,000) (WN 1)	(1,18,800)	1,81,200
Interest credited to Provident Fund Account at 10%	60,000	
Less : Exempted u/s 10(14) upto 9.5%	57,000	3,000
Entertainment Allowances		30,000
Children Education Allowance (₹ 5,000×3)	15,000	
Less : Exempt u/s 10(14) [₹ 300 p.m.×12 months × 2 Children (maximum)]	(7,200)	7,800
Taxable Salary before Perquisites		13,12,000
Value of Perquisites		
Rent Free Unfurnished Accommodation		
Least of the following—		
Rent paid by the Employer 70,000		
15% of Salary [15% of ₹ 11,27,800] (WN 2) (assumed that Mumbai population > 25 Lakhs as per latest census)	1,69,170	70,000
Gross Salary		13,82,000
Less : Deduction u/s 16		
Entertainment Allowance u/s 16(ii) [Not a Govt. Employee]		Nil
Income under the head Salary		13,82,000
Gross Total Income		13,82,000
Less : Deduction Under Chapter VI-A		
U/s 80C LIC Premium paid 15,000		
Contribution to PF Account 3,00,000		
U/s 80CCC Contribution to Pension Fund 12,000		
[The maximum amount along with deduction 1,00,000 u/s 80CCC and 80CCC or u/s 80C, restricted to ₹ 1,00,000]		
U/s 80CCF Subscription to long term Infrastructure Bond 20,000		
U/s 80D Medical Insurance Premium paid 20,000	20,000	
U/s 80G (WN 3) 63,450	63,450	(2,03,450)
Total Income		11,78,550

Computation of Tax Liability

Particulars	₹	₹
Total Income		11,78,550
Upto ₹ 1,90,000		NIL
1,90,000 – 5,00,000 = @ 10% of 3,10,000		31,000
5,00,000 – 8,00,000 = @ 20% of 3,00,000		60,000
8,00,000 – 11,78,550 = @ 30% of 3,78,550		1,13,565
		<u>2,04,565</u>
(+) Deduction Cess @ 2%	4,091	
(+) SHEC @ 1%		2,046
		<u>2,10,702</u>
Rounded off u/s 288A		<u>2,10,700</u>

Working Notes :

- Salary for the purpose of computation of Taxable Portion of Employer's Contribution to Provident Fund
= Basic Salary + DA considered for Retirement Benefits + Commission
= ₹ 6,00,000 + ₹ 2,40,000 + ₹ 1,50,000 = ₹ 9,90,000
- Salary for the purpose of computation of Taxable Value of Rent Free Unfurnished Accommodation
= Basic Pay (+) D.A (forming part of Salary) (+) All other Taxable Allowances (+) Any other monetary benefits
= 6,00,000 + 2,40,000 + 1,00,000 + 1,50,000 + 30,000 + 7,870 = 11,27,800
- Computation of deduction u/s 80G :**

50% of least of the followings :

	₹
(a) Amount Donated	2,00,000
(b) 10% of Adjusted Gross Total Income	
Gross Total Income	13,82,000
Less : Deduction under Chapter VI-A excluding sec. 80G	
u/s 80C	
80CCC	1,10,000
(retired u/s 80CCF)	
u/s 80CCF	20,000
u/s 80D	20,000

STUDY NOTE - 5

INCOME FROM HOUSE PROPERTY

This Study Note includes

- Chargeability
- Deemed Owner
- Property Income is Exempt from Tax to Certain Persons
- Recovery of Unrealised Rent
- Receipt of Arrears of Rent
- Unrealized Rent
- Municipal Tax
- Deduction from Net Annual Value
- Computation of Prior Period Interest
- Computation of Income from House Property
- Computation

5.1 CHARGEABILITY [Section 22]

1. The basis of chargeability under the head income from house property is **Annual Value**.
2. The property must consist of Building or Lands Appurtenant thereto.
3. The assessee must be the owner of such property.
4. The property may be used for any purpose other than the assessee's business or profession.

5.2 DEEMED OWNER [Section 27]

1. **Owner:** An Individual shall be considered as owner of a property when the document of title to the property is registered in his name.
2. **Deemed Owner:** Under the following circumstances, Income from House Property is taxable in the hands of the Individual, even if the property is not registered in his name —
 - (a) Where the Property has been transferred to **spouse for inadequate consideration** other than in pursuance of an agreement to live apart.
 - (b) Where the Property is transferred to a **minor child for inadequate consideration (except a transfer to minor married daughter)**
 - (c) Where the Individual holds an **impartible estate**.
 - (d) Where the Individual is a **member** of Co-operative Society, Company, or other Association and has been allotted a house property by virtue of his being a member, even though the property is registered in the name of the Society / Company / Association.
 - (e) Where the property has been transferred to the individual's name as part-performance of a contract u/s 53A of the Transfer of Property Act, 1882. (i.e. Possession of the Property has been transferred to Individual, but the Title Deeds have not yet been transferred).
 - (f) Where the Individual is a **holder of a Power of Attorney** enabling the right of possession or enjoyment of the property.
 - (g) Where the property has been constructed on a **leasehold land**.
 - (h) Where the **ownership** of the Property is under **dispute**.



- (i) Where the property is taken on a lease for a period of not less than 12 years, then the lessee shall be deemed as the owner of the property.

5.3 PROPERTY INCOME IS EXEMPT FROM TAX TO CERTAIN PERSONS

10(19A):	An Ex-Ruler for his occupation (palace)
10(20):	Local Authority.
10(21):	Approved Scientific Research Association.
10(23B):	Institution for the development of Khadi and Village Industries.
10(23BB):	Khadi and Village Industries Boards.
10(23BBA):	A body or authority for administering religious or charitable Trust or endowments.
10(23C):	Certain Funds, educational institutions, hospitals etc.
10(24):	Registered Trade Union.
10 (26B):	Statutory Corporation or an institution or association financed by the Government for promoting in the interests of members of SC or ST.
10(27) :	Co-operative Society for promoting the interest of the members of SC or ST.
11 :	Charitable Trust.
13A :	Political Party.

5.4 RECOVERY OF UNREALISED RENT [SECTION 25AA]

- Chargeability:** Recovery of Unrealized Rent is chargeable to tax as “Income from House Property”.
- Year of Taxability:** Unrealized Rent recovered is taxable in the financial year in which it is recovered.
- Non-Subsistence of Ownership:** It will be taxable in the hands of Individual even if he does not own the property to which such rent pertains.
- Deduction:** No deduction will be allowed against such receipt.

5.5 RECEIPT OF ARREARS OF RENT [SECTION 25B]

- Meaning:** Arrears of Rent means the incremental rent relating to earlier financial years which has not been offered to tax in those financial years itself, but received during the current financial year,
- Chargeability:** Receipt of Arrears of Rent will be chargeable to tax under the head Income from House Property only.
- Year of receipt:** It is taxable as income of the financial year in which he receives the arrears of rent.
- Non-subsistence of ownership:** It is taxable in the hands of the Individual even if he does not own the prop” at the time of receipt of arrears of rent.
- Deduction:** A standard deduction of 30% of the amount of arrears received will be allowed as deduction.

5.6 UNREALIZED RENT (Rule 4)

Unrealized Rent means the rent not paid by the tenant to the owner and the same shall be deducted from the Actual Rent Receivable from the property before computing income from that property, provided the following conditions are satisfied :

- The tenancy is bonafide
- The defaulting tenant should have vacated the property
- The assessee has taken steps to compel the defaulting tenant to vacate the property

4. The defaulting tenant is not in occupation of any other property owned by the assessee
5. The assessee has taken all reasonable steps for recovery of unrealised rent or satisfies the Assessing Officer that such steps would be useless.

5.7 MUNICIPAL TAX

1. **Municipal Tax includes** services tax like Water Tax and Sewerage Tax levied by any local authority. It can be claimed as a deduction from the Gross Annual Value of the Property.
2. **Conditions:**
 - (a) **Paid by Owner.** The tax shall be borne by the owner and the same was paid by him during the previous year.
 - (b) **Property let out:** Municipal Tax can be claimed as a deduction only in respect of let out or deemed to be let out properties (i.e. more than one property self occupied).
 - (c) **Year of payment:** Municipal Tax relating to earlier previous years, but paid during the current previous year can be claimed as deduction only in the year of payment.
 - (d) **Advance Taxes:** Advance Municipal Tax paid shall not be allowed as deduction in the year of payment, but can be claimed in the year in which it falls due.
 - (e) **Borne by Tenant:** Municipal taxes met by tenant are not allowed as deduction.
3. **Foreign Property:** For a property situated outside India, Municipal Tax levied by foreign Local Authority can be claimed as a deduction.

5.8 DEDUCTION FROM NET ANNUAL VALUE

A. Standard Deduction u/s 24(a)

Standard deduction of 30% of NAV (Net Annual Value) shall be allowed to the assessee.

B. Interest on Loan u/s 24(b)

1. **Purpose of loan:** The loan shall be borrowed for the purpose of **acquisition, construction, repairs, renewal or reconstruction of the house property.**
2. **Accrual basis:** The interest will be allowed as a deduction on accrual basis, even though it is not paid during the financial year.
3. **Interest on interest:** Interest on unpaid interest shall **not be allowed as a deduction.**
4. **Brokerage:** Any brokerage or commission paid for acquiring the loan **will not be allowed as a deduction.**
5. **Prior period interest:** Prior Period Interest shall be allowed in **five equal installments commencing from the financial year in which the property was acquired or construction was completed.**

Note : Prior period interest means the interest from the date of borrowal of the loan upto the end of the financial year immediately preceding the financial year in which acquisition was made or construction was completed.

6. **Interest on fresh loan to repay existing loan:** Interest on any fresh loan taken to repay the existing loan **shall be allowed as a deduction. [Circular 28 / 20.9.1969]**
7. **Inadmissible interest:** Interest payable outside India without deduction of tax at source and in respect of which no person in India is treated as an agent u/s 163 shall **NOT** be an allowable **expenditure. [Section 25]**
8. **Certificate:** The assessee should furnish a **certificate from the person from whom the amount is borrowed.**

5.9 COMPUTATION OF PRIOR PERIOD INTEREST

Let us illustrate the steps with an example :

Loan taken on 1.7.08 ₹8,00,000 @ 9% p.a. Date of completion of construction 31.5.11. Loan amount remains outstanding till date. Determine Prior Period and Interest u/s 24(b)

Step 1:	Identify the Date of Borrowal of Loan	1.7.08 (P.Y : 08-09)
Step 2:	Identify the Date of Completion / Acquisition	31.5.11 (P.Y : 11-12)
Step 3:	Identify Last Date of the Financial Year immediately preceding the date of Completion / Acquisition.	31.3.11 (P.Y : 10-11)
Step 4:	Prior Period = Calculated Period from Step 1 to Step 3	= 1.7.08-31.3.11 = 33 months
Step 5:	Prior Period Interest = Prior Period as per Step 4 × Rate of interest × Amount of Loan	$= \frac{33}{12} \times \frac{9}{100} \times 8,00,000 = 1,98,000$
Step 6:	Allowable Prior Period Interest = Prior Period Interest as per Step 5 / 5	= 39,600

Current Year Interest = 8,00,000 × 9% × 12 months = 72,000

∴ In to u/s 24(b) = CYI + 1/5 PCPI

$$\begin{aligned}
 &= 72,000 + \frac{1}{5} \times 1,98,000 \\
 &= 72,000 + 39,600 \\
 &= 1,11,600
 \end{aligned}$$

COMPUTATION OF INCOME FROM HOUSE PROPERTY

PROPERTY USED FOR	ANNUAL VALUE	Deductions Allowed	Section
1. Self occupied House Property or self occupied property kept vacant	Nil	u/s 24(b), subject to the fulfillment of conditions	23(2)
2. Property let out for the whole year	To be computed	All deductions	23(1)(a)/(b)
3. Let out property kept vacant for the whole year	Nil	All deductions except Sec. 24(a)	23(1)(c)
4. Let out property kept vacant for the part of the year	To be computed	All deductions	23(1)(c)
5. Two or more self-occupied House Property. Compute as if they are let-out property. Take the combination which will minimize total income from house property. <ul style="list-style-type: none"> One property at the option of the assessee to be treated as self-occupied Other property/(ies) shall be deemed to have been let out 	Nil	To be computed Sec.24(b), subject to the fulfillment of conditions All Deductions 23(4)	23(1)(a)/(b)

COMPUTATION OF INCOME FROM HOUSE PROPERTY

GROSS ANNUAL VALUE	xx
Less: Municipal Taxes paid during the year	xx
NET ANNUAL VALUE	xx
Less: Standard Deduction @ 30% of NAV u/s 24(a)	xx
Less: Interest on Loan u/s 24(b)	xx
Add: Recovery of Unrealized Rent u/s 25 AA	xx
Income from House Property before considering Arrears of Rent	xx
Add: Arrears of Rent Received	xx
Less: Deduction u/s 25B: 30% of Arrears Received	xx
NET INCOME FROM HOUSE PROPERTY	xx

COMPUTATION OF GROSS ANNUAL VALUE

1. Municipal Value	xx
2. Fair Rental Value or Notional Rental Value	xx
3. Higher of (1) and (2)	xx
4. Standard Rent (if applicable)	xx
5. Reasonable Expected Rent = Lower of Step (3) and (4)	xx
6. Annual Rent (total rent assuming the property to be let out throughout the previous year)	xx
7. Deduct: Unrealized Rent as per Rule 4	xx
8. Actual Rent = Step (6) – (7)	xx
9. Higher of Reasonable Expected Rent (Step 5) & Actual Rent (Step 8)	xx
10. Deduct: Vacancy Allowance (proportionately on the basis of Annual Rent in Step 6)	xx
11. GROSS ANNUAL VALUE	xx

TERMINOLOGIES USED

- (a) **Municipal Value :** It is the value that the municipal authorities deem as the value of the property for the purpose of assessment of property taxes. We shall have to ascertain the Gross Municipal Value. If Net Municipal Value is given, we shall have to determine the Gross Municipal Value = [Net Municipal Value + $\frac{1}{9}$ th of Net Municipal Value]

In case of Metro cities, Municipal Tax is calculated on the Net Municipal Value = [Gross Municipal Value – 10% of Gross Municipal Value].

Net Municipal Value is also known as **Net Rateable Value**.

If the information is silent regarding Municipal value, whether gross or net, we shall always consider it to be Gross Municipal Value, so as to give the maximum benefit to the Assessee.

- (b) **Fair Rent:** It is the rent of the property fetched by a similar property in the same or similar locality with the same facilities.
- (c) **Standard Rent:** It is the maximum rent which a person can recover from the tenant under the Rent Control Act.

CONDITIONS FOR ADMISSIBILITY OF INTEREST ON LOAN TAKEN FOR SELF-OCCUPIED PROPERTY

- Loan taken for acquisition or construction of house property on or after 01.04.99 and the same was completed within 3 years from the end of the financial year in which capital was borrowed, interest paid or payable, subject to a maximum of ₹ 1,50,000 (= **Current year + $\frac{1}{5}$ th of prior-period interest**)
- Loan taken **prior to 1.4.99** for acquisition or construction or loan taken for repair, renovation or reconstruction at any point of time, interest paid or payable subject to a maximum of ₹ 30,000 (= **Current year + $\frac{1}{5}$ th of prior-period interest**)
- Loan taken **on or after 1.4.99** for acquisition or construction of house property, and the **same was not completed within 3 years** from the end of the financial year in which capital was borrowed, interest paid or payable, subject to a maximum of ₹ 30,000 (= **Current year + $\frac{1}{5}$ th of prior-period interest**)

ILLUSTRATIONS ON INCOME FROM HOUSE PROPERTY

Illustration 1. Mr. Rohan owns two houses. Their particulars for the Previous year 2011-2012 are given below:

Particulars	House I	House II
	Construction completed on 1.04.2011	
	Self-occupied	Let out
	₹	₹
Municipal valuation	10,00,000	15,00,000
Fair rent	12,00,000	14,00,000
Standard rent	8,00,000	16,00,000
Annual rent received /receivable	Nil	18,00,000
Municipal taxes paid	1,20,000	150,000
Insurance premium paid	10,000	15,000
Repair expenses	1,50,000	2,00,000
Unrealised rent-conditions of Rule 4 satisfied	Nil	4,50,000
Interest on loan for the pre-construction period	3,00,000	4,50,000
Interest on loan for the post construction period for the PY year 2010-2011	1,00,000	1,50,000
Date of borrowing the loan	31.12.2005	31.12.2005
Certificate of interest attached to the return.	No	No

Determine the income from house property for the assessment year 2012-2013.

Would you change your answer if construction is completed on 31-3-2012 and interest certificate is also attached?

Solution : **Computation of Income from House Property for the AY 2012-2013**

Particulars	House No. I-Self-occupied		House No. II-Let out	
	Date of completion 1-4-2011 failing after 3 years from the end of FY in which loan was taken	Date of completion 31-3-2011 within 3 years from the end of FY in which loan was taken	House No. II-Let out Interest certificate/Date of competing construction are not relevant.	
	Interest certificate not relevant (a)	Interest certificate attached (b) (I)	Interest certificate not attached (b)(ii)	
	₹	₹	₹	₹
Gross annual value				
(a) ALV	Nil	Nil	Nil	15,00,000
(b) Annual rent received excluding unrealised rent	Nil	Nil	Nil	13,50,000
Whichever is higher, is GAV	Nil	Nil	Nil	15,00,000
Less : Municipal taxes paid	Nil	Nil	Nil	(-) 1,50,000
Net annual value	Nil	Nil	Nil	13,50,000
Less : Permissible deductions :				
Less : (I) Statutory deduction : 30% of Net annual value	Nil	Nil	Nil	(-) 4,05,000
(ii) Interest on loan	(-) 30,000	(-) 1,50,000	(-) 30,000	(-) 2,40,000
Income from house property	(-) 30,000	(-) 1,50,000	(-) 30,000	7,05,000

Note :

1. Interest for House No. I-Self-occupied:

- (a) (i) Interest for pre-construction period $\div 5 : 3,00,000 \div 5 = ₹ 60,000$
(ii) Interest for post-construction period : ₹ 1,00,000
(i) + (ii) = ₹ 1,60,000

Where loan is taken on or after 1.04.1999 but the house is not completed within 3 years from the end of the financial year in which the loan was taken, maximum ceiling of interest, eligible for deduction is only ₹ 30,000. It is operative from the AY 2005-2006 and subsequent years.

In the instant case, self-occupied house is completed after the prescribed time-limit of 3 years. Hence, deduction is restricted to ₹ 30,000.

- (b) (i) In the, instant case, self-occupied house has been completed within 3 years from the end of the financial year in which loan was taken and certificate of interest is also attached. Hence, interest on loan, subject to the maximum ceiling of ₹ 1,50,000 has been allowed.
(ii) construction is completed within the prescribed time-limit of 3 years from the end of the FY which loan was taken but interest certificate is not attached. Hence, interest on loan, subject to a maximum of ₹ 30,000, has been allowed.

2. Interest for House No. II. Deduction has been worked out as under :

- (i) Interest for pre-construction period : $4,50,000 \div 5 = 90,000$
(ii) Interest for post-construction period during 2007-2008 : 1,50,000
Interest eligible for deduction (i) + (ii) = 2,40,000

3. No deduction is available for insurance premium and repair expenses incurred.

Illustration 2. Mr. Shyam owns two houses, which are occupied by him for his own residence.

The detailed particulars of houses and his other incomes for the previous year 2011-12 are given below:

Particulars	House A ₹	House B ₹
Fair rent	5,00,000	5,00,000
Municipal value	4,20,00	4,50,000
Standard rent	4,50,000	6,20,000
Municipal taxes paid	50,000	60,000
Interest on loan for the FY 2011-12	1,60,000	2,20,000
Date of loan	1.12.2001	1.04.2002
Date of completion	31.03.2003	31.03.2005
Certificate of interest attached with return of income	No	Yes
Mr. Shyam earns income from other sources amounting to ₹ 2,00,000		

Compute his total income and advise him which house should be opted for self-occupation.

Solution : **Computation of Income from House Property under different options**

Particulars	House A ₹	House B ₹
(a) Assuming both properties are self-occupied (SO)		
Annual value	Nil	Nil
Less : Interest on loan	(-) 30,000	(-) 1,50,000
Loss from house property	(-) 30,000	(-) 1,50,000
(b) Assuming both properties as deemed let out (DLO)		
Gross annual value	4,20,000	6,00,000
Less : Municipal taxes paid	(-) 50,000	60,000
Net annual value	3,70,000	5,40,000
Less : Permissible deduction :		
(i) Statutory deduction : 30% of Net annual value	(-) 1,11,000	(-) 1,62,000
(ii) Interest on loan	(-) 1,60,000	(-) 2,20,000
Income from house property	99,000	1,58,000
(c) Criteria for selection of house for self-occupied : Lowest taxable income	Option I	Option II
Income from house A	(-) 30,000	99,000
Income from house B	1,58,000 (DLO)	(DLO) (SO)
Income from other sources	2,00,000	2,00,000
Total income	3,28,000	1,49,000

Conclusion : House B should be treated as self-occupied.

Illustration 3. Dr. (Ms) Priyanka is the owner of a big house consisting of three units. Unit I consist of 40% area and Unit II and III are equal dimension, each occupying 30% area. The construction of house was completed on 1 April 2006 at a cost of ₹ 10,00,000. The municipal value of the house for the previous year 2011-12 has been fixed at ₹ 2,00,000. Municipal taxes have been levied and paid @ 15% of rateable value. The rent under the Rent Control Act is ₹ 1,50,000. Unit I is let out @ 10,000 p.m. for residential purposes. Unit II is self-occupied. Unit III is used by her for her professional purposes. The rent did not pay two months rent and conditions of Rule 4 are satisfied. She paid ground rent, ₹ 9,000; interest on loan, taken during 2002-2003 for the construction of the house and payable during the PY 2011-2012 ₹ 1,50,000; insurance premium, ₹ 6,000. She spent ₹ 30,000 on repair of the house. Depreciation for the clinic portion is ₹ 15,000. Her gross receipt from professional during the previous year 2011-2012 amount to ₹ 5,60,000.

Compute her gross total income for the assessment year 2012-2013.

Solution :

Computation of Income from House Property for the Assessment Year 2012-2013

Particulars	House Let-out ₹	House Self-occupied ₹
Gross annual value :		
(a) ALV : House let out		
(i) 40% of municipal value : ₹ 80,000 or		
(ii) 40% of the standard rent : ₹ 60,000		
ALV is restricted to ₹ 60,000		
(b) Actual rent for 40% portion for 10 months : ₹ 1,00,000	1,00,000	Nil
Gross annual value		
Less : Municipal taxes paid by the owner for 40%		
Portion Rs. 2,00,000 × $\frac{15}{100} \times \frac{40}{100}$ = Rs. 12,000	12,000	Nil
Net annual value	88,000	Nil
Less : Deduction from net annual value (Sec. 24)		
1. Statutory deduction : 30% of net annual value	(-) 26,400	
2. Interest on loan : 40% of ₹ 1,50,000	(-) 60,000	(-) 30,000
Taxable income	1600	(-) 30,000
Computation of taxable income from profession :		
Gross professional income		5,00,000
Less : Expenses for 30% portion used for profession		
1. Municipal taxes Rs. 2,00,000 × $\frac{15}{100} \times \frac{30}{100}$ (Sec. 30)	9,000	
2. Repair : 30% of ₹ 30,000 (Sec. 30)*	9,000	
3. Ground rent : 30% of ₹ 9000 (Sec. 30)*	2,700	
4. Interest on loan : 30% of ₹ 1,50,000 [Sec. 36(1)(iii)]*	45,000	
5. Insurance premium : 30% of ₹ 6000 (Sec.30)*	1,800	
6. Depreciation (Sec. 32)	15,000	
	<u>82,500</u>	<u>82,500</u>
		<u>4,17,500</u>
Computation of total income :		
1. Income from house property :		
(a) Let out	1600	
(b) Self-occupied	(-) 30,000	
	<u>(-) 28,400</u>	<u>(-) 28,400</u>
2. Income from profession		4,17,500
Gross Total Income/Total Income		<u>3,89,100</u>



Illustration 4. Mr. Ranjit Sinha is employed with HUDCo. Ltd. @ ₹ 25,000 p.m. He is the owner of a house property construction of which was completed on 1 April 2003. Since then, it has been in his self-occupancy for residential purposes. The particulars in respect of the house for financial year 2011-2012 are given below :

	₹
Municipal valuation	2,00,000
Municipal tax paid	20,000
Ground rent outstanding	5,000
Insurance premium paid	

Interest on loan, taken on 1-6-2010 for renovation of the house, is ₹ 75,000 for the year 2011-2012. However, he could pay only, ₹ 45,000 during the year. He is transferred in February 2012 to the Nagpur Branch of the Company. He intends to allow his sister to occupy the house free of rent in his absence. He seeks your advice in this connection. Compute his total income for AY 2012-2013.

Solution :

Computation of Total Income

Assessee : Mr. Ranjit Sinha

A. Y : 2012-13

Particulars	Case I House kept Vacant ₹	Case II House is occupied by his sister in his absence ₹
Income from house property :		
Gross annual value	Nil	2,00,000
Less : Municipal taxes paid	Nil	(-) 20,000
Net annual value	Nil	1,80,000
Less : Permissible deduction (Sec. 24)		
(i) Statutory deduction – 30% of Net annual value	Nil	(-) 54, 000
(ii) Interest on loan for renovation	(-) 30,000	(-) 75,000
Income from House Property	(-) 30,000	51,000
Statement of total income :		
Income from salary	3,00,000	3,00,000
Income from house property	(-) 30,000	51,000
Total Income	2,70,000	3,51,000

Advise : From tax angle it is not advisable to allow his sister to occupy the house in his absence.

Illustration 5. Mr. Kalidas is the owner of a house property. Its municipal valuation is ₹ 3,00,000. It has been let out for ₹ 4,40,000. The local taxes payable by the owner amount to ₹ 30,000 but as per agreement between the tenant and the landlord, the tenant has paid them direct to the municipality. The landlord, however, bears the following expenses on tenants amenities during the year 2011-2012.

	₹
Expenses of water connection	10,000
Water charges	20,000
Lift maintenance	15,000
Salary of gardener	18,000
Lighting of stairs	6,000
Maintenance of swimming pool	12,000
The landlord claims the following deductions :	
Repairs	30,000
Land revenue paid	6,000
Collection charges	10,000

Compute the taxable income from the house property for the assessment year 2012-13

Solution :

Computation of Income from House Property

Assessee : Mr. Kalidas

A.Y : 2012-13

Particulars	₹	₹
Gross annual value to be higher of the following :		
(a) ALV : Municipal valuation : 3,00,000		
Or		
(b) Actual rent : 3,69,000 (see note below)		3,69,000
Whichever is higher, is GAV		Nil
Less : Local taxes payable ₹ 30,000 :		3,69,000
Net annual value		1,10,700
Less : Statutory deduction : 30% of net annual value		2,58,300
Taxable income		4,40,000
Note : Composite rent		
Less : Value of the amenities provided by the assessee :		
(i) Water connection expenses : Not allowed being capital expenditure	—	
(ii) Water charges	20,000	
(iii) Lift maintenance	15,000	
(iv) Salary of gardener	18,000	
(v) Lighting of stairs	6,000	
(vi) Maintenance of swimming pool	12,000	(-) 71,000
Actual rent		3,69,000



Illustration 6. Mr. M.Saha is the owner of a house in Kolkata consisting of three identical floors, (ground floor, first floor and second floor). Ground floor is let out and the rest is occupied by him for his residence. The full particulars of the house for the previous year 2011-2012 are given below:

Particulars	₹
(i) Municipal valuation	12,00,000
(ii) Fair rent	5,00,000
(iii) Standard rent	Nil
(iv) Annual rent of the ground floor	6,00,000
(v) Municipal taxes paid by J	1,50,000
(vi) Water/sewerage benefit tax, paid to Kolkata Municipal Corporation	70,000
(vii) House remains vacant for 2 months :	
(viii) Unrealized rent, condition of Rule 4 are satisfied	2,50,000
(x) Interest on loan, taken for the purchase of the house in April 2010 as per certificate	2,70,000

Compute the income from the house property for the AY 2012-2013.

Solution :

Computation of Income from House Property

Assessee : Mr. M. Saha

AY 2012-2013

Particulars	Ground floor ₹	I & II floor in self-occupancy ₹
Gross annual value		
(a) ALV	5,00,000	Nil
(b) Actual rent received / receivable	2,50,000	Nil
Even without vacancy, actual rent received is lower than the ALV: 6,00,000-2,50,000 = 3,50,000. Thus, the loss is not wholly due to vacancy. Hence, only loss due to vacancy is to be deducted from ALV to determine GAV. GAV is (5,00,000-1,00,000)	4,00,000	Nil
Less : Municipal taxes paid	(-) 50,000	Nil
Net annual value	3,50,000	Nil
Less :		
(1) Statutory deduction – 30% of AV.	(-)1,05,000	—
(2) Interest on loan	(-) 90,000	(-) 1,50,000
Income from house property	1,55,000	(-) 1,50,000

Illustration 7. Mr.Ashis discloses the following particulars of the property owned by him during the PY 2011-2012.

Particulars	House self-occupied	Flat allotted by HB Society let out ₹	Shops & godowns let out ₹
Municipal value	5,00,000	2,00,000	4,00,000
Fair rent	4,00,000	2,50,000	5,00,000
Municipal taxes payable	60,000	80,000	80,000
(a) Paid by Ashis	60,000	30,000	-
(b) Paid by tenant	-	50,000	80,000
Annual rent	-	3,60,000	7,00,000
Expenses incurred by Ashis :	-		
Maintenance charges	-	12,000	-
Repairs	-	-	2,60,000
Collection charges	-	-	6,000
Electricity bills paid	-		Nil
Insurance premium	20,000	-	6,000
Ground rent	5,000	2,000	6,00
Depreciation	1,000	2,000	20,000

Other information :

- He has taken the loan on 1 July 2009 to purchase the house in self-occupancy. However, he could purchase the house on 1 May 2009. He repaid ₹ 6,30,000 on 1 July 2011. This includes a charge of ₹ 1,20,000 on account of interest from the date of borrowing.
- The flat has been purchased under EMI scheme of the Gujarat Apartment Cooperative House Building Society Ltd. He has to pay 120 EMI of ₹ 10,000 each, which includes 50% charge on account of interest. He has defaulted in payment of the last 20 EMI. To repay the outstanding EMI and penal interest of Rs, 20,000, he borrowed ₹ 2,20,000 on 1 October 2011 @ 15% p.a.

The flat remained vacant for 1.5 months and rent of 3/4th month could not be realised. Conditions of Rule 4 have been satisfied,

- Shops and godowns are held as stock-in-trade. However, till a suitable buyer is found, these are let out. P claims that income from letting should be computed under the head “profits and gains of business of profession”.

He has borrowed money to construct/repair the godowns/shops. He paid ₹ 20,000 on account of brokerage for arranging the loan.

Interest is payable outside India, in two equal instalments of ₹ 50,000 each. The first instalment was paid net of tax at ₹ 40,000. However, the second instalment was paid without deducting tax at sources as the recipient had given an undertaking in the prescribed form to pay the tax. Compute income from house property for the assessment year 2012-2013.

Solution :
Computation of Income from House Property
A. Y : 2012-13

Particulars	House self-occupied ₹	Flat let-out ₹	Shops and godowns let out ₹
Gross Annual Value	Nil	2,92,500	7,00,000
Less: Municipal taxes paid by the assessee	—	30,000	—
Net Annual Value	Nil	2,62,500	7,00,000
Less: Deductions u/s 24			
Statutory deduction u/s 24(a) @ 30% of NAV	—	78,750	2,10,000
Interest on Loan u/s 24(b)	24,000	37,500	50,000
Income from House Property	(24,000)	1,46,250	4,40,000

Workings:
1. Gross Annual Value:

ALV	2,50,000
Annual Rent	3,60,000
Less: Vacancy Allowance	45,000
Unrealised rent	<u>22,500</u>
	<u>2,92,500</u>

The higher of ALV and Annual rent, is the Gross Annual Value ₹2,92,500

2. Interest on loan taken for self- occupied:

- Amount of interest = ₹1,20,000
- Period of interest = 01.07.2007 to 01.07.2009 = 2 years
- Pre-acquisition period = 01.07.2007 to 31.3.2009 = 9 months
- Interest for pre-acquisition period = $1,20,000 \times 9/24$
- Interest for 2007-2008 = ₹ $1,20,000/2$ = ₹60,000
- Interest for 2008-2009 for 3 months = $1,20,000 \times 3/24$ = 15,000
- Interest deductible during PY 2009-2010 = $(45,000/5) + (15,000)$ = 24,000

3. Interest for the flat:

- Interest included in EMI from 01.04.2010 to 30.09.2010:
₹ $(10,000 \times 6/2)$ = ₹ 30,000
- Interest on money borrowed to repay original loan interest
₹ $(10,000 \times 20/2) = (1,00,000 \times 15\% \times 1/2)$ = 7,500
- Total interest = ₹ $(30,000 + 7,500)$ = ₹ 37,500
- No deduction is allowed for penal interest.

4. Letting out of shops and godowns, held as stock-in-trade:

Section 22 excludes from its charge only such building as is occupied by the assessee for his business or profession, profits of which are chargeable to tax.

In the instant case, as letting out is not the business of the assessee, so, it cannot be said that he has occupied shop and godown for his business. Accordingly, income from letting out shop and building, held as stock-in-trade is assessable under the head “income from house property”.

Where an assessee is not holding shops and godowns as stock-in-trade but engaged in the business of letting them on hire, the income is again chargeable under the head “house property” as it is a specific head of income dealing with letting out of buildings only.

5. Deduction in respect of other expenses: Section 24 does not allow any deduction in respect of (i) maintenance charges, (ii) repairs, (iii) collection charges, (iv) electricity, (v) fire insurance premium, (vi) ground rent, and (vii) depreciation.

Illustration 8. Puja has occupied three houses for his self-occupancy. Their particulars for the previous year 2011-2012 are given below:

Particulars	House X ₹	House Y ₹	House Z ₹
Municipal value	3,60,000	9,60,000	9,50,000
Municipal taxes paid	40,000	80,000	90,000
Fair rent	5,40,000	8,00,000	10,00,000
Standard rent	4,50,000	6,00,000	9,00,000
Repairs	1,50,000	2,50,000	3,00,000
Ground rent paid	20,000	25,000	30,000
Insurance premium paid	5,000	6,000	7,000
Interest on loan taken for purchase of H.P.	75,000	1,20,000	2,00,000
Year of the loan	1997-98	2000-2001	2005-06

She has suffered loss in his business, amounting ₹ 3,00,000

Compute her total income, advising her which house should be specified for self-occupancy concession:

Solution : Computation of income from house property under different options :

(a) Assuming all the properties are self-occupied (SO)	House X (SO) ₹	House Y (SO) ₹	House Z (SO) ₹
Annual value	Nil	Nil	Nil
Less: Interest on loan	30,000	30,000	1,50,000
Loss from house property	30,000	30,000	1,50,000

(b) Assuming all the properties as Deemed Let Out (DLO)	House X (DLO) ₹	House Y (DLO) ₹	House Z (DLO) ₹
Gross annual value	4,50,000	6,00,000	9,00,000
Less: Municipal taxes paid	40,000	80,000	90,000
Net annual value	4,10,000	5,20,000	8,10,000
Less: Statutory deduction u/s 24(a) @ 30% of net annual value	1,23,000	1,56,000	2,43,000
Interest on Loan u/s 24(b)	(-) 75,000	(-) 1,20,000	(-) 2,00,000
Income from house property	2,12,000	2,44,000	3,67,000

(c) Total Income under different options for self-occupancy:

Particulars	Option 1 House X ₹	Option 2 House Y ₹	Option 3 House Z ₹
House X	(-) 30,000 (SO)	2,12,000 (DLO)	2,12,000 (DLO)
House Y	2,44,000 (DLO)	(-) 30,000 (SO)	2,44,000 (DLO)
House Z	3,67,000 (DLO)	3,67,000 (DLO)	(-) 1,50,000 (SO)
Income from house property:	5,81,000	5,49,000	3,06,000
Loss from business	(-) 3,00,000	(-) 3,00,000	(-) 3,00,000
Total income	2,81,000	2,49,000	(-) 6,000

Conclusion: A house with minimum income/maximum loss should be opted for self-occupancy concession to minimise the tax liability.

The option can be changed from year to year.

In the instant case, House Z should be treated as self-occupied. There will be no tax-liability, and the assessee will carry forward the unabsorbed business loss of ₹ 94,000 for next 8 assessment years.

Illustration 9. Mr. Pradipto completed construction of a residential house on 1.4.2011. Interest paid on loans borrowed for purpose of construction during the 2 years prior to completion was ₹ 40,000. The house was let-out on a monthly rent of ₹ 4,000. Annual Corporation Tax paid is ₹ 2,000. Interest paid during the year is ₹ 16,000. Amount spent on repairs is ₹ 2,000. Fire Insurance Premium paid is ₹ 1,500 p.a. Property was vacant for 3 months. Annual letting value as per corporation records is ₹ 30,000. Compute the income under the head "Income from House Property" for the A.Y. 2012-13.

Solution :

Assessee : Mr. Pradipto

Previous Year : 2011-2012

Assessment Year : 2012-13

Computation of Income from House Property

Particulars	₹	₹
Gross Annual Value u/s 23(1)(c) (Note 1)		36,000
Less : Municipal Taxes Paid		(2,000)
Net Annual Value (NAV)		34,000
Less : Deduction u/s 24 —		
(a) 30% of Net Annual Value (₹ 30,000 × 30%)	9,000	
(b) Interest on Borrowed Capital :		
Interest for Current Year ₹ 16,000		
Interest of Prior Period (₹ 40,000 × 1/5) ₹ 8,000	24,000	(33,000)
Income from House Property		1,000

Note :

Computation of Gross Annual Value

Municipal Value	30,000
Annual Rent (4,000 × 12)	48,000
(-) Unrealised Rent	Nil
Annual Rent	48,000
Higher of MV & Actual Rent	48,000
Less : Vacancy Allowance	
$\frac{48,000}{12} \times 3$	12,000
Gross Annual Value	36,000

Illustration 10. Mr. Suman owned a house property at Chennai which was occupied by him for his residence. He was transferred to Mumbai in June 2011 and therefore he let-out the property with effect from 1.7.2011 on a monthly rent of ₹ 5,000. The corporation tax payable in respect of the property was ₹ 10,000 of which 50% was paid by him before 31.3.2012. Interest on money borrowed for the construction amounted to ₹ 20,000. Compute the income from house property for the A.Y. 2012-13.

Solution :

Assessee : Mr. Suman

Previous Year : 2011-2012

Assessment Year : 2012-13

Computation of Income from House Property

Particulars	₹	₹
Annual Value u/s 23(1)(a)/(b) – Rent receivable for the whole year		60,000
Less : Municipal Taxes paid ₹ 10,000 × 50%		(5,000)
Net Annual Value		55,000
Less : Deduction u/s 24		
(a) 30% of Net Annual Value ₹ 55,000 × 30%	16,500	
(b) Interest on borrowed Capital	20,000	(33,500)
Income from House Property		21,500

Illustration 11. Mr. G and N constructed their houses on a piece of land purchased by them at Kolkata. The built-up area of each house was 1,000 sq ft. Ground floor and an equal area in the First floor. Mr. G started construction on 1.7.2010. Mr. G occupied the entire house on 1.4.2011. Mr. N occupied the Ground floor on 1.7.2011 and let-out the first floor for a rent of ₹ 20,000 p.m. However, the tenant vacated the house on 31.12.2010 and Mr. N occupied entire house during 1.1.2012 to 31.3.2012.

Following are the other information :

- | | |
|---|-----------------|
| (i) Fair Rental Value of each unit (Ground floor/First floor) | ₹ 2,00,000 p.a. |
| (ii) Municipal Value of each unit (Ground floor/First floor) | ₹ 90,000 p.a. |
| (iii) Municipal taxes paid by | G – ₹ 12,000 |
| | N – ₹ 12,000 |
| (iv) Repair and Maintenance charges paid by | G – ₹ 40,000 |
| | N – ₹ 50,000 |

Mr. G has availed a housing loan of ₹ 16.00 Lakhs @ 12% p.a. on 1.4.2010. N has availed a housing loan of ₹ 18.00 Lakhs @ 10% p.a. on 1.7.2010. No repayment was made by either of them till 31.3.2012. Compute Income from House Property for G and N for the A.Y. 2012-13.



Solution :

Assessee : Mr. G

Previous Year : 2011-2012

Assessment Year : 2012-13

Computation of Income from House Property

Particulars	₹
Nature : Self Occupied – Annual Value u/s 23(2)	NIL
Less : Deduction u/s 24 : Interest – ₹ 16 Lakhs × 12% = ₹ 1,92,000 (Restricted to ₹ 1,50,000)	1,50,000
Loss from House Property	(1,50,000)

Note : Since construction of property is completed in the year of borrowal of loan itself, prior period interest does not arise.

Assessee : Mr. N

Previous Year : 2011-2012

Assessment Year : 2012-13

Computation of Income from House Property

Particulars	₹	₹	₹
Ground Floor Nature : Self Occupied			NIL
Annual Value u/s 23(2)			
Less : Deduction u/s 24 : Interest on Borrowed Capital			
Current Year : ₹ 18,00,000 × 10% × 50%	90,000		
Prior Period : ₹ 18,00,000 × 10% × 9/12 × 50% × 1/5	13,500	(1,03,500)	(1,03,500)
First Floor Nature : Let-Out			
Annual Value u/s 23(1)(a)/(b)			
Higher of Fair Rent vs. Municipal Rent [See Note 1]	1,50,000		
Higher of Rent selected above vs. Actual Rent received [See Note 2]	1,80,000	1,80,000	
Less : Municipal Taxes – (₹ 12,000 × 50%)		(6,000)	
Net Annual Value		1,74,000	
Less : Deduction u/s 24			
(a) 30% of Net Annual Value	52,200		
(b) Interest on borrowed Capital			
Current Period Interest – (₹ 18,00,000 × 10% × 50%)	90,000		
Prior Period Interest – (₹ 18,00,000 × 10% × 9/12 × 50% × 1/5)	13,500	(1,55,700)	18,300
Net Income from House Property			(85,200)

Note :

- Since the construction of property was completed on 1.7.2010, Fair rent, Municipal Rent and Actual Rent receivable are to be considered only for a period of **9 months**.

$$\text{Fair Rent} = 2,00,000 \times \frac{9}{12} = 1,50,000$$

$$\text{Municipal Value} = 90,000 \times \frac{9}{12} = 67,500$$

- Since the house is self occupied for part of the year and let out for part of the year, income from house property shall be calculated for the whole year as deemed let out property. Therefore Rent receivable is ₹ 1,80,000 (₹ 20,000 × 9).

Illustration 12. Mr. L is the owner of a commercial property let out at ₹ 30,000 p.m. The municipal tax on the property is ₹ 15,000 annually, 60% of which is payable by the tenant. This tax was actually paid on 15.4.2012. He had borrowed a sum of ₹ 10 Lakhs from his cousin, resident in USA (in dollars) for the construction of the property on which interest at 18% is payable. He has also received arrears of rent of ₹ 40,000 during the year, which was not charged to tax in the earlier years. What is the Property Income of X for A.Y. 2012-13?

Solution :

Assessee : Mr. L

Previous Year : 2011-2012

Assessment Year : 2012-13

Computation of Income from House Property

Particulars	₹	₹
Let Out : So, Annual Value u/s 23(1)(a)/(b) = Actual Rent = ₹ 30,000×12		3,60,000
Less : Municipal Taxes Paid during the F.Y. 2010-11		NIL
Net Annual Value		3,60,000
Less : Deduction u/s 24		
– 30% of NAV –	₹ 3,60,000 × 30%	1,08,000
– Interest on Housing Loan (Note)	₹ 20,00,000 × 8%	1,60,000
		(2,68,000)
Income from House Property before considering Arrears of Rent		92,000
Arrears of Rent Received	40,000	
Less : Deduction u/s 25B – 30% of Arrears received – ₹ 40,000 × 30%	(12,000)	28,000
Net Income from House Property		64,000

Note : It is presumed that the tax has been deducted at source on the amount of interest payable outside India.



STUDY NOTE - 6

PROFITS AND GAINS OF BUSINESS OR PROFESSION

This Study Note includes

- Definition of Business and Profession
- Chargeability
- Computation of Income from Business or Profession

6.1 DEFINITION OF BUSINESS AND PROFESSION

BUSINESS [Sec. 2(13)]

Definition of “Business” includes any trade, commerce or manufacture or any adventure or concern in the nature of trade, commerce or manufacture.

Certain terms used in the definition can be understood as follows:

“Trade” is the activity of purchase and sale of goods with an object of making profit.

“Commerce” means trade repeated on a large scale.

“Manufacture” is said to have taken place when as a result of certain process(es) applied on a product, a new and commercially different product comes into existence which is known to the market as different from the raw material.

“Adventure or concern in the nature of trade, commerce or manufacture” has to be decided on the basis of cumulative effect of the facts and circumstances of each case i.e. scale of activity, time period covered by it, nature of the commodity etc. in order to decide whether the act is an adventure or concern.

Business necessarily means a continuous activity with a profit motive by the application of labour and skill.

Under certain circumstances a single and isolated transaction may also constitute business provided it bears clear indications of trade or is an adventure in the nature of trade.

PROFESSION [Sec. 2(36)]

Profession involves an exercise of intellect and skill based on learning and experience. It includes “vocation”.

Vocation refers to any work performed on the strength of one's natural ability for that work. Regularity and profit-motive are not necessary for an activity to be called a vocation.

6.2 CHARGEABILITY [Sec. 28]

The following incomes shall be chargeable under this head :-

U/s 28, the following income shall be chargeable to income-tax under the head “Profits and gains of business or profession”,—

- (i) the profits and gain of any business or profession which was carried on by the assessee at any time during the previous year;
- (ii) any compensation or other payment due to or received by, —
 - (a) any person, by whatever name called, managing the whole or substantially the whole of the affairs of an Indian company, at or in connection with the termination of his management or the modification of the terms and conditions relating thereto;

- (b) any person, by whatever name called, managing the whole or substantially the whole of the affairs in India of any other company, at or in connection with the termination of his office or the modification of the terms and conditions relating thereto ;
- (c) any person, by whatever name called, holding an agency in India for any part of the activities relating to the business of any other person, at or in connection with the termination of the agency or the modification of the terms and conditions relating thereto ;
- (d) any person, for or in connection with the vesting in the Government, or in any corporation owned or controlled by the Government, under any law for the time being in force, of the management of any property or business ;
- (iii) income derived by a trade, professional or similar association from specific services performed for its members ;
 - (a) profits on sale of a licence granted under the Imports (Control) Order, 1955, made under the Imports and Exports (Control) Act, 1947 (18 of 1947) ;]
 - (b) cash assistance (by whatever name called) received or receivable by any person against exports under any scheme of the Government of India ;]
 - (c) any duty of customs or excise re-paid or re-payable as drawback to any person against exports under the Customs and Central Excise Duties Drawback Rules, 1971 ;]
 - (d) any profit on the transfer of the Duty Entitlement Pass Book Scheme, being the Duty Remission Scheme under the export and import policy formulated and announced under section 5 of the Foreign Trade (Development and Regulation) Act, 1992 (22 of 1992);]
 - (e) any profit on the transfer of the Duty Free Replenishment Certificate, being the Duty Remission Scheme under the export and import policy formulated and announced under section 5 of the Foreign Trade (Development and Regulation) Act, 1992 (22 of 1992) ;]
- (iv) the value of any benefit or perquisite, whether convertible into money or not, arising from business or the exercise of a profession ;]
- (v) any interest, salary, bonus, commission or remuneration, by whatever name called, due to, or received by, a partner of a firm from such firm :

Exception :

where any interest, salary, bonus, commission or remuneration, by whatever name called, or any part thereof has not been allowed to be deducted under clause (b) of section 40, the income under this clause shall be adjusted to the extent of the amount not so allowed to be deducted ;

- (va) any sum, whether received or receivable, in cash or kind, under an agreement for—
 - (a) not carrying out any activity in relation to any business; or
 - (b) not sharing any know-how, patent, copyright, trade-mark, licence, 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 provision for services :

Exception : this sub-clause (a) shall not apply to—

- (i) any sum, whether received or receivable, in cash or kind, on account of transfer of the right to manufacture, produce or process any article or thing or right to carry on any business, which is chargeable under the head “Capital gains”;
- (ii) any sum received as compensation, from the multilateral fund of the Montreal Protocol on Substances that Deplete the Ozone layer under the United Nations Environment Programme, in accordance with the terms of agreement entered into with the Government of India.

Explanation : For the purposes of this clause,—

- (i) “agreement” includes any arrangement or understanding or action in concert,—
 - (A) whether or not such arrangement, understanding or action is formal or in writing; or
 - (B) whether or not such arrangement, understanding or action is intended to be enforceable by legal proceedings;



- (ii) “service” means service of any description which is made available to potential users and includes the provision of services in connection with business of any industrial or commercial nature such as accounting, banking, communication, conveying of news or information, advertising, entertainment, amusement, education, financing, insurance, chit funds, real estate, construction, transport, storage, processing, supply of electrical or other energy, boarding and lodging;
- (vi) any sum received under a Keyman insurance policy including the sum allocated by way of bonus on such policy.

Explanation : For the purposes of this clause, the expression “Keyman insurance policy” shall have the meaning assigned to it in clause (10D) of section 10;

- (vii) any sum, whether 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 under section 35AD.

Speculative Business :

Where speculative transactions carried on by an assessee are of such a nature as to constitute a business, the business (hereinafter referred to as “speculation business”) shall be deemed to be distinct and separate from any other business.

In the context of computation of income under the head profits and gains of Business or Profession, the following points may be noted :

- (a) Profits chargeable to tax are computed on the basis of commercial principles including generally accepted accounting principles and practices.
- (b) Only profits or gains are liable to income-tax and not mere gross receipts. Capital receipts and Capital expenditures are not generally to be taken into account while computing profits under this section unless it expressly provides in the provisions of the Income Tax Act.
- (c) Taxable profits or gains should be real and not notional. Anticipated losses are not provided for and unrealized gains are not considered except in case of stock valuation which is valued at lower of cost or market price.
- (d) Profits and gains arises to Business or Profession carried on by the assessee are computed in relation to a time period which is covered by a previous year.

It is not necessary that Business or Profession should be carried on throughout the Previous Year. However, as an exception, the following incomes are taxable by virtue of express provisions under the Act even if no business was carried on during the Previous Year.

- (i) Recovery against any loss, expenditure or trading liability earlier allowed as deduction. [sec. 41(1)]
 - (ii) Balancing charge i.e. profits or gains from sale of a building, machinery, plant or furniture owned by a power undertaking. [Sec. 41(2)]
 - (iii) Profits and gains from sale of capital asset used for scientific research. [Sec. 41(3)]
 - (iv) Recovery against bad debt. [Sec. 41(4)]
 - (v) Amount withdrawn from special reserve. [Sec. 41(4A)]
 - (vi) Profits and gains from transfer of the Business or interest in the petroleum and natural gas business. [Sec. 42(2)]
 - (vii) Any sum received after the discontinuance of a business. [Sec. 176(3A), Sec. 176(4)]
- (e) Profits and gains can not arise by trading with oneself.
 - (f) Taxability of an income depends on its source. Thus, profits and gains that arise to an assessee during the Previous Year may not be taxed under the head Business or Profession, its taxability depends on source.

For example :

- (i) Profits from activity of purchasing and selling real estate properties is taxable under the head “Profits and gains of Business or Profession”. However, rental income from any of such properties is taxable under the head “Income from House Property”.



- (ii) Interest on securities held as investment is charged to tax under the head “Income from Other Sources”. However, interest on securities held as stock-in-trade is charged under the head “Profits and gains of Business or Profession”.
- (g) Profits and gains from illegal business are also chargeable to Income-tax under this head.
- (h) Income from letting or exploiting of commercial assets is charged under the head Business or Profession but the intention of the assessee should be to treat the asset as commercial asset.

6.3 COMPUTATION OF INCOME FROM BUSINESS OR PROFESSION (Sec. 29)

Format for Computation of Business or Profession Income :

Computation of Income from Business

Net Profit as per Profit & Loss Account	xxx
<i>Add :</i> Expenses disallowed/Inadmissible Expenses [i.e. items already debited in P/L A/c but not eligible for deduction]	xxx
<i>Less :</i> Incomes Credited in P/L A/c to be treated separately under difference heads of income	(xxx)
<i>Less :</i> Expenses allowed as per Provisions	(xxx)
Income from Business	xxx

Computation of Income from Profession

Receipts relating to Profession (on Cash Basis)	xxx
<i>Less :</i> Payment relating to profession (both cash and accrual basis)	(xxx)
Income from Profession	xxx

Expenses which are allowed as deduction [Sections 30 to 37]

RENT, RATES, TAXES, REPAIRS AND INSURANCE FOR BUILDINGS [Sec. 30]

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 ;
- (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]

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



DEPRECIATION [Sec. 32]

Depreciation is the diminution in the value of an asset due to normal wear and tear or due to obsolescence. In order to allow depreciation as notional expenses in computing profits and gains of Business or Profession, the following conditions are to be fulfilled;

- (i) **There must be assets** : It may be classified into two types.
 - (a) **Tangible assets** : Buildings, machinery plant or furniture.
 - (b) **Intangible assets** : Know-how, patents, copy rights, trademarks, licences, franchise or any other business or commercial right of similar nature acquired on or after 1st April, 1998.
- (ii) **Such asset should be owned, wholly or partly, by the assessee** : Ownership does not necessarily mean legal ownership. Assessee will be treated as owner if he is capable of enjoying the right of the owner in respect of asset in his own right and not on behalf of the owner in whom title vests even though a formal deed of title has not been executed and registered (Mysore minerals, Ltd. vs. CIT[(1999) 239 ITR 775(SC)]). In case of a building in which Business or Profession is carried on is not owned by the assessee but he holds a lease or other right of occupancy though he is not entitled to depreciation on the building, depreciation is allowed on the capital expenditure incurred for the purposes of Business or Profession on construction of any structure or renovation etc.
- (iii) **Such asset should be used for purposes of Business or Profession**

Depreciation Statement as per Income Tax Act, 1961

Particular of Asset	WDV as on 01.4.....	Additions at Actual Cost	Deductions	Net Value of Block	Depreciation for Current Year	WDV as on 31.03.....
1	2	3	4	5	6	7

BLOCK OF ASSETS [Sec. 2(11) AND EXPLANATION 3 TO SECTION 32] :

It means a group of assets falling within a class of assets comprising,

- (i) **Tangible assets** : Buildings, machinery, plant or furniture;
- (ii) **Intangible assets** : Know-how, patents, copyright, trademarks, licences, franchises or any other business or commercial rights of similar nature in respect of which same percentage of depreciation has been prescribed.

Aligning the definition of 'Block of Asset' [Explanation 3 to section 32(1)] [W.e.f. A.Y. 2010-11]

The term "block of assets" has been defined in section 2(11) and in *Explanation 3* to section 32(1) of the Income-tax Act. However, these definitions are not identical and therefore they are subject to misuse. Accordingly, *Explanation* of section 32(1) has been amended so as to delete the definition of "block of assets" provided therein. Consequently, "block of assets" will derive its meaning only from section 2(11) and *Explanation 3* shall contain the meaning of assets which shall be applicable for electricity undertaking only.

WRITTEN DOWN VALUE [Sec. 43(6)]

- (i) In case of assets acquired in the Previous Year, written down value is the actual cost to the assessee.
- (ii) In case of assets acquired before the Previous Year :- Written down value is the actual cost of the asset to the assessee as reduced by depreciation actually allowed to him in respect of such asset under this Act.
- (iii) In case of any block of assets :- Written down value of the block of asset is computed as per the following mechanism.

	₹
Written down value of the block of assets at the beginning of the current Previous Year.	***
Add: Actual cost of assets falling within that block, acquired during the Previous Year.	***
Less: Moneys payable and scrap value if any, in respect of asset sold/discarded/demolished destroyed during the Previous Year	***
Written down value	***

- (iv) In case of block of assets when there is a slump sale:- In accordance with section 2(42C), “slump sale” means the transfer of one or more undertakings as a result of the sale for lump sum consideration without values being assigned to the individual assets and liabilities in such sales.

Written down value in case of slump sale is computed as per the following mechanism.

	₹
Written down value of the entire block at the beginning of the relevant Previous Year.	***
Add: Actual cost of assets falling within that block, acquired during the Previous Year.	***

Less: Moneys payable and scrap value if any, in respect of asset sold/discarded/demolished/destroyed during the Previous Year	***

Less: Actual cost of the asset falling within that block as reduced by amount of depreciation actually allowed to such asset, but it should not exceed the written down value of the block as at the end of the Previous Year in it cannot be negative.	***
Written down value in case of slump sale.	***

- (v) Written down value in case of demerged company [Explanation 2A of Sec. 43(6)]:

Written down value of resulting company =	Written down value of assets prior to demerger shall be reduced by the written down value of assets transferred pursuant to demerger.
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- (vi) Written down value in case of resulting company [Explanation 2B to Sec. 43(6)]

Written down value of resulting company =	Written down value of assets as appearing in the books of the demerged company before the demerger.
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- (vii) Written down value in case of corporatisation [Explanation Sec. 5 to Sec. 43(6)]

Written down value of a company under a =	Written down value of the transferred asset by a scheme of corporatisation approved by SEBI recognised stock exchange in India immediately before such transfer.
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Note : Written down value cannot be negative i.e. it shall be reduced to ‘nil’ in the following situations :

- Where the block of assets ceases to exist i.e., all the assets of the block are transferred.
- Where a part of the block is sold and the sale consideration of the assets sold exceeds the value of the block.

Written down value where the assessee was not required to compute his total income of any earlier previous year [Explanation 6* to section 43(6) inserted by the Finance Act, 2008, w.r.e.f assessment year 2003-2004]

Where an assessee was not required to compute his total income for the purposes of this Act for any previous year or years preceding the previous year relevant to the assessment year under consideration,—

- the actual cost of an asset shall be adjusted by the amount attributable to the revaluation of such asset, if any, in the books of account;
- the total amount of depreciation on such asset, provided in the books of account of the assessee in respect of such previous year or years preceding the previous year relevant to the assessment year under consideration shall be deemed to be the depreciation actually allowed under this Act for the purposes of this clause; and



- (c) the depreciation actually allowed under clause (b) shall be adjusted by the amount of depreciation attributable to such revaluation of the asset.

Computation of written down value where income of an assessee is derived in part from agriculture and in part from business chargeable to income-tax under the head "Profits and gains of business or profession" [Explanation 1 to Section 43(6)] [W.e.f. A.Y. 2010-11]

Section 32(l)(iii) provides that depreciation is to be allowed and computed at the prescribed percentage on the written down value (WDV) of any block of assets. Sub-clause (b) of clause (6) of section 43 provides that WDV in the case of assets acquired before the previous year shall be computed by taking the actual cost to the assessee less all depreciation "actually allowed" to him under the Income-tax Act.

Rules 7A, 7B and 8 of the Income tax Rules, 1962, deal with the computation of composite income where income is derived in part from agricultural operations and in part from business chargeable to tax under the Income tax Act, 1961 under the head "Profits & Gains of Business". These rules prescribe the method of computation in the case of manufacture of rubber, coffee and tea. In such cases, the income which is brought to tax as "business income" is a prescribed fixed percentage of the composite income.

The Hon'ble Supreme Court in the case of *CIT vs. Doom Dooma India Ltd* 222 CTR 105 (SC) has held that in view of the language employed in sub-clause (b) of clause (6) of section 43 regarding depreciation "actually allowed", where any income is partially agricultural and partially chargeable to tax under the Income-tax Act, 1961 under the head "Profits & Gains of Business", the depreciation deducted in arriving at the taxable income alone can be taken into account for computing the WDV in the subsequent year.

For instance, Rule 8 prescribes the taxability of income from the manufacture of tea. Under the said rule, income derived from the sale of tea grown and manufactured by seller shall be computed as if it were income derived from business, and 40% of such income shall be deemed to be income liable to tax. As a result of the Court decision, the resultant computation of depreciation is as per the following illustration :

	₹
Sale proceeds of tea	5,000
Less: Expenses:	
Depreciation - (10% of ₹ 5,000)	(500)
Others expenses	(1,500)
Composite income	3,000
Income subject to charge under the Income-tax Act, 1961 by application of rule 8 (40% of 3,000)	1,200
Income not chargeable to income-tax (60% of 3,000)	1,800

According to the interpretation of the Court, the W.D.V. of the fixed asset for the immediately succeeding year is to be taken at ₹ 4,800 (₹ 5,000 minus ₹ 200 being depreciation allocated for business income) and not ₹ 4,500 (₹ 5,000 minus depreciation of ₹ 500 allowed for determining composite income). Thus the depreciation for which deduction is allowed to the assessee while computing its agricultural income is to be ignored for computing the W.D.V. of the asset according to the Court ruling.

The above interpretation is not in accordance with the legislative intent. WDV is required to be computed by deducting the full depreciation attributable to composite income. Hence in the above illustration, the WDV of the fixed asset for the immediately succeeding year is to be taken at ₹ 4,500 and not 4,800 as held by the Supreme Court. The ambiguity in this case has arisen on account of the interpretation of the meaning of the phrase "actually allowed" in sub-clause (b) of clause (6) of section 43.

Therefore Explanation 7 has been inserted in section 43(6) to provide that where the income of an assessee is derived, in part from agriculture and in part from business chargeable to income-tax under the head "Profits and gains of business or profession", for computing the written down value of assets acquired before the previous

year, the total amount of depreciation shall be computed as if the entire income is derived from the business of the assessee under the head "Profits and gains of business or profession" and the depreciation so computed shall be deemed to be the depreciation actually allowed under this Act.

MONEYS PAYABLE [EXPLANATION TO SEC. 41]

Moneys payable in respect of any building, machinery, plant and furniture includes

- (a) any insurance, salvage or compensation moneys payable in respect thereof;
- (b) where the building, machinery plant or furniture is sold, the price for which it is sold.

DEPRECIATION MANDATORY

Explanation 5 to Sec. 32 inserted by the Finance Act, 2001 w.e.f. 1.4.2002, it is clarified that the depreciation provisions shall apply, whether or not the assessee has claimed the deduction in respect of depreciation in computing his total income.

ADDITIONAL DEPRECIATION :

Sec. 32(1)(iia) has been inserted by the Finance Act, 2002 w.e.f. from Assessment Year 2003-04 to provide additional depreciation @20% of the actual cost of new machinery and plant (other than ships and air craft) which has been acquired and installed after the 31.3.2002 by an assessee engaged in the business of manufacture or production of any article or thing provided that such further deduction of 20% shall be allowed to :

- (i) a new industrial undertaking during any Previous Year in which such undertaking begins to manufacture or produce any article or thing on or after 1.4.2002. or
- (ii) any industrial undertaking existing before the 1.4.2002, during any Previous Year in which it achieves the substantial expansion by way of increase in installed capacity by not less than 25% provided further that no deduction shall be allowed in respect of :
 - (a) any machinery or plant which, before its installation by the assessee was used either within or outside India by any other person; or
 - (b) any machinery or plant installed in office premises for any residential accommodation including accommodation in the nature of a guest house; or
 - (c) any office appliances or road transport vehicles; or
 - (d) any machinery or plant, the whole of the actual cost 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 one Previous Year.

Additional depreciation as per section 32(1)(iia) is available on furnishing the details of machinery or plant and increase in the installed capacity of production in the prescribed form along with the returned income and the report of an accountant as defined in the explanation below subsection (2) of section 288 certify that the deduction has been correctly cleaned in accordance with the provisions of this clause.

Illustration 1 : The WDV of plant and machinery on 1.4.2011 of Z Ltd. engaged in manufacturing of PVC granules is ₹ 2000 lacs. Company purchased additional plant and machinery for ₹ 1,600 lacs on 18.4.2011 inclusive of second-hand machine imported from Ireland of ₹ 400 lacs to increase its installed capacity of production from 1000 TPA to 1500 TPA. The production from new machine commenced w.e.f 1.12.2011. Work out by giving reasons the amount of allowable depreciation.

Assessee : Z Ltd.

Previous Year : 2011-12
Computation of Depreciation

Assessment Year : 2012-13

Particulars	Lakhs	
	₹	₹
Opening WDV		2,000
Add : Additions During the year		1,600
Net Value for the purpose of Depreciation		3,600
Less : Depreciation of the Year		
— On Opening Block – ₹ 2,000 Lakhs × 15%	300	
— On Additions (Period of usage less than 180 days) — ₹ 1,600 lakhs × 15% × 50%	120	
— Additional Depreciation on Eligible Assets (Notes)	120	540
Closing WDV		3,060

Notes :

1. Second hand machinery imported from China is not an eligible asset for the purpose of Additional Depreciation computation. Therefore, cost of eligible assets = ₹ 1,600 lakhs – ₹ 400 lakhs = ₹ 1,200 lakhs.
2. Period of usage of new machine is less than 180 days. Therefore, they are entitled to only 50% of additional depreciation rate of 20%.

DEPRECIATION AT REDUCED RATE

Where an asset referred in clause (i) or clause (iii) as the case may be, is acquired by the assessee during the Previous Year and is put to use for the purposes of Business or Profession for less than 180 days in that Previous Year, the depreciation allowable in respect of such asset shall be restricted to 50% of the normal rate.

Illustration 2 :

W.D.V. of Machinery (Rate of Depreciation @15%) = ₹ 5,00,000

New Machinery Purchased (on 31.12.11) = ₹ 1,00,000, having same rate of depreciation.

Calculate : Depreciation u/s 32

Block A : Machinery
(Rate of Depreciation = 15%)

W.D.V. of the Machinery	5,00,000
Add : Cost of New Asset Purchased (relating to the Block) [Put to Use > 180 Days]	Nil
Less : Government Subsidy Received for Purchase/Acquisition Asset	Nil
Less : Adjustment for CENVAT Credit	Nil
Less : Sale of Asset from the Block	Nil
W.D.V for Charging Depreciation	5,00,000
Less : Depreciation @ 15%	75,000
Closing WDV	4,25,000

Block B : Machinery

(Rate of Depreciation = 7.5% of 15%, since Acquired & Put to Use for less than 180 Days)

Cost	1,00,000
Less : Depreciation @ 7.5%	7,500
Closing WDV	92,500

Total Depreciation u/s 32 = 75,000
7,500
82,500

TERMINAL DEPRECIATION [Sec. 32(1)(iii)]

Terminal Depreciation (i.e. Loss on Transfer) & Balancing Charge (i.e. Gain on Transfer)

- Applicable for any undertaking engaged in generation or generation and distribution of power;
- It must be a depreciable asset, on which depreciation is claimed on straight line basis;
- Such depreciable asset, is sold, discarded, demolished or destroyed in a previous year

If there arises:

- Loss on Sale = Terminal Depreciation;
- Gain on Sale = Balancing Charge.

Calculation of Terminal Depreciation:

- Calculate Written Down Value of the depreciable asset on the first day of the previous year in which such asset is sold, discarded, demolished or destroyed.
- Ascertain Net Sale Consideration.

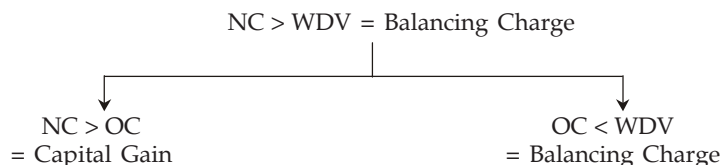
If value as per (1) > value as per (2) = Loss = Terminal Depreciation

Note:

- Sale Consideration is money payable to the tax payer in respect of such depreciable asset (+) Scrap Value, if any
- Net Sale Consideration = Sale Consideration (-) Expenses on Transfer;
- Sale consideration is the actual money, received or receivable in cash or by cheque or draft;
- It excludes any other thing or benefit which can be measured and converted in terms of money;
- If the asset is sold or discarded, etc, in the previous year in which it is first put to use, any loss on transfer of that asset shall be treated as capital loss and not as terminal depreciation;
- The asset must be used by the assessee for the purpose of business or profession, at least for some considerable time period during the previous year, in which the transfer/sale takes place;
- Terminal depreciation can only be allowed, if the asset is completely written off from the books of accounts.

Balancing Charge u/s 41(2) and Capital Gain u/s 50A:

If value as per (2) > value as per (1) = Gain = Balancing Charge



Where,

- NC = Net Sale Consideration
 OC = Original Cost
 WDV = Written Down Value


Illustration 3 :

Kalpataru power Projects is a power generating unit. On 1.4.2009, it purchased a plant of ₹ 50,00,000, eligible for depreciation @15% on SLM. Compute balancing charge or terminal depreciation assuming the plant is sold on 21.4.2011 for : (a) ₹ 8,50,000 (b) ₹ 32,00,000 (c) ₹ 45,00,000 (d) ₹ 52,00,000

Solution :

Computation of Terminal depreciation or balancing charge, capital gain.

Particulars	A	B	C	D
W.D.V. as on 1.4.2011	35,00,000	35,00,000	35,00,000	35,00,000
Less: Sale Proceeds	8,50,000	32,00,000	45,00,000	52,00,000
Balance	26,50,000	30,00,000	(10,00,000)	(17,00,000)
Terminal depreciation	26,50,000	3,00,000	NIL	NIL
Balancing charge	NIL	NIL	10,00,000	15,00,000
Short term capital Gain	NIL	NIL	NIL	2,00,000
Computation of Depreciation:				
Original cost	50,00,000			
Less: Depreciation	7,50,000			
WDV as on 1.4.2010	42,50,000			
Less : Depreciation for the year 2010-2011	7,50,000			
WDV as on 1.4.2011	35,00,000			

SECTION 43(1) — ACTUAL COST

Actual Cost [Sec. 43 (1)] for the purpose of determination of Depreciation

Explanation	Nature of Acquisition	Actual Cost
1	Assets used in scientific research subsequently put into use for the business	NIL
2	Asset received under gift, will or inheritance	WDV to the previous owner
3	Acquisition of asset to claim depreciation on enhanced cost to reduce tax liability	Cost as determined by the Assessing Officer with the prior approval of Joint Commissioner of Income Tax
4	Transfer and re-acquisition of the same asset	Least of the followings: (i) WDV at the time of original transfer (ii) Re-purchase price
4A	Sale and Lease Back	WDV to the transferor
5	Building previously used for private purpose	Cost of Acquisition or construction Less : Deemed Depreciation Deemed depreciation refers to the total depreciation that would have been allowable had the building been used for business purpose since its acquisition
	Succession of business	WDV to the previous owner

6	Transfer by Parent company to its wholly owned Indian subsidiary company	WDV to Parent company
	Transfer by wholly owned Indian subsidiary company to its Indian Parent company	WDV to Indian Subsidiary company
7	Amalgamation (amalgamated company must be an Indian company)"	WDV to the amalgamating company
7A	Demerger : In the hands of the Demerged Company after demerger	WDV of Demerged Co. before Demerger <i>Less</i> : WDV of assets transferred to Resulting Co.
7A	Demerger: In the hands of the Resulting Company	WDV to Demerged Company
8,9,10	Asset acquired by the Assessee	Cost of Acquisition <i>Add</i> : (i) Interest on loan for the period upto the date of usage of the asset (ii) Freight & Insurance (iii) Loading, Unloading Charges (iv) Installation Charges <i>Less</i> : (i) Government Subsidy or Grant received related to purchase of asset (ii) CENVAT credit
11	Assets brought into India by a Non-resident	Actual cost of Acquisition <i>Less</i> : Notional depreciation for the period such asset was held outside India
12	Asset acquired by a company under a scheme of Corporatisation of Recognized Stock Exchange	Actual Cost as if there is no such corporatization.

Note:

The followings are to be considered for determination of Actual Cost

- (i) Actual cost refers to the cost of the asset to the assessee;
- (ii) Interest on loan after commencement of commercial production should not be included in the Actual cost;
- (iii) Trial Run expenses should be included in Actual Cost, after adjusting any income derived during the trial run period;
- (iv) All expenses directly attributable (e.g. salaries, guest house for staff engaged in installation activities , travelling expenses incurred) to setting up of plant and machinery, will be included;
- (v) Loss arising out of exchange rate differences, should be included in Actual Cost;
- (vi) Subsidy received from Government for units in backward areas should not be adjusted against actual cost of project, for computing depreciation;
- (vii) Cost of land shall not be considered for claiming depreciation;
- (viii) Interest receipts and Hire charges received from Contractors should be reduced from Actual Cost;
- (ix) Conversion cost incurred for transforming an asset shall be included in actual cost;

- (x) Interest earned on deposits made to open Letter of Credit for purchase of any asset will be adjusted to reduce actual cost.

Treatment of Trial Run Expenses and Income earned during Trial run period
Illustration 4 :

X Ltd. acquired a printing machine for ₹ 25,00,000. Transport Cost, including loading and unloading charges ₹ 35,000. Expenses incurred during the trial run period ₹ 2,00,000. Output generated during trial run period was sold for ₹ 90,000. Depreciation @ 15% . Compute WDV. Would your answer differ if the output generated during trial run period was ₹ 3,00,000.

Assessee : X Ltd

Previous Year : 2011-12

Computation of Depreciation

Particulars	Amount (₹)	Amount (₹)
Expenses incurred during trial run period	2,00,000	2,00,000
Less : Income from sale of output generated during trial run period	(90,000)	(3,00,000)
Net Cost / Gain	1,10,000	(1,00,000)
Actual Cost of the Machine	25,35,000	25,35,000
Add : Net Cost during trial run	1,10,000	—
Less : Net Gain during trial run		(1,00,000)
Actual Cost of Machine for charging depreciation	26,45,000	24,25,000
Less : Depreciation @ 15%	3,96,750	3,63,750
Written Down Value (W.D.V.)	22,48,250	20,61,250

Treatment of Currency Exchange Fluctuation
Illustration 5 :

Z Ltd. purchased machinery (rate of depreciation 15%) from Japan for US\$ 2,50,000 on 17. 08.2010 (US \$ = 43.25) by borrowing from Hero Bank Ltd. Z Ltd. took a forward contract on 11.07.2010, when the exchange rate was ₹ 45.70 per US\$. This was put to use from 23.11.2010. Compute Depreciation for the previous years 2010-11 and 2011-12.

Assessee: Z Ltd

Previous Year : 2010-11 & 2011-12

Computation of Depreciation and Written Down Value

Particulars	Amount (₹)
Cost of the Asset (US\$ 2,50,000 × ₹ 43.25)	1,08,12,500
Less : Depreciation @ 50% of 15% (since Put to Use < 180 days) for previous year 2010-11 (₹ 1,08,12,500 × 50% × 15%)	(8,10,938)
WDV as on 01.04.2011	1,00,01,562
Add : Exchange Rate Difference [US\$ 2,50,000 × ₹ (45.70 – 43.25)]	6,12,500
WDV for claiming depreciation	1,06,14,062
Less : Depreciation @ 15% for the previous year 2011-12 (₹ 1,06,14,062 × 15%)	15,92,109
WDV as on 01.04.2012	90,21,953

CENVAT Credit Adjustment

Illustration 6 :

Pharma Ltd. imported machinery from Germany on 27.8.11 at a cost of ₹ 40 crores. Customs Duty paid @ 20%. Government granted subsidy of ₹ 25 crores. The entire logistics was supported by Nexgen Courier Ltd., an Indian Company. Total Service charges paid to them ₹20 lacs including service tax of ₹ 2,20,000.

Compute Actual Cost, if assessee, avail CENVAT credit adjustment.

Assessee : Pharma Ltd

Previous Year : 2011-12

Computation of Depreciation and Written Down Value

Particulars	Amount (₹ crores)
Cost of Purchase	40.00
Add: Customs Duty @ 20% on ₹ 40 crores	8.00
Less: Government subsidy granted	25.00
Less: CENVAT Credit (Service Tax paid included in the payment made to Nexgen Courier Ltd.)	0.22
Actual Cost for the purpose of charging depreciation	22.78

Illustration 7 :

ZED Ltd. imported machinery from South Korea on 12.5.2011 for US\$ 50,000. Exchange rate on that date : US\$ = ₹ 44. 70. Customs Duty paid @ 20%. Government granted subsidy of ₹ 15,00,000. The assessee had a forward contract on 2.4.2011 at US\$ 45.30. Logistics services was provided by Carrywell Courier Ltd. Service Charges paid ₹ 2,00,000 including service tax of ₹ 25,000. Engineers and labourers were engaged at site for installation of the machinery. Salary and wages paid for site engineers and labourers including their travelling expenses amounted to ₹ 4,60,000. Expenses incurred during trial run period ₹ 1,50,000. Sale of output produced during trial run period ₹ 90,000. Interest earned on deposits made to open Letter of Credit for purchase of this machinery ₹ 15,000 . The machine was put to use from 05.10.11. Depreciation @ 15%. Compute Actual Cost and Written Down Value.

Assessee: ZED Ltd.

Previous Year : 2011-12

Computation of Actual Cost and Written Down Value

Particulars	Amount (₹ crores)
Cost of the Asset (US\$ 50,000 × ₹ 44.70)	22,35,000
Add : Customs Duty paid @ 20% on ₹ 22,35,000	4,47,000
Less : Government Subsidy granted	(15,00,000)
Add : Exchange Rate Difference [US\$ 50,000 × ₹ (45.30 - 44.70)]	30,000
Add : Transportation charges paid ₹ 2,00,000 (including Service Tax ₹ 25,000)	2,00,000
Less : CENVAT credit adjustment (credit for Service tax included in service charges paid to Carrywell Courier Ltd.)	(25,000)
Add : Installation expenses incurred for payment of site engineers & labourers including travelling expenses	4,60,000
Add : Expenses incurred during trial run period	1,50,000
Less : Sale of output generated during trial run period	(90,000)
Less : Interest earned on deposits made to open Letter of Credit for purchase of this machinery	(15,000)
Actual Cost for the purpose of determining depreciation	18,92,000
Less : Depreciation @ 50% of 15% (since Put to Use < 180 days) for previous year 2011-12 (₹ 18,92,000 × 50% × 15%)	1,41,900
WDV as on 01.04.2012	17,50,100



PROPORTIONATE DEPRECIATION

In the following cases, depreciation is allowed on proportionate basis where in any Previous Year, there is :-

- Succession of a partnership firm by a company [u/s. 47(xiii)] or
- Succession of a proprietary concern by a company [u/s. 47(xiv)]
- Succession of any business other than on death [u/s. 170] or
- Amalgamation of company [u/s. 2(1B)] or
- Demerger of any company [u/s. 2(19AA)]

Depreciation : Adjustments required after Succession of Business

Illustration 8 : Conversion of Sole-proprietorship into Company

A Bros., a sole-proprietorship concern, was converted into a A Ltd. on 20.9.2011. Before the conversion, the concern had a block of furniture (rate of depreciation @ 10%), whose WDV as on 01.04.2011 was ₹ 6,50,000. On 01.05.2011, a new furniture of the same block was purchased for ₹ 50,000. A Ltd. purchased another furniture of the same type on 20.12.2010 for ₹ 48,000. Compute depreciation that would be claimed by A Bros. and A Ltd for the previous year 2011-12.

Solution :

- Depreciation shall have to be calculated at the prescribed rates, as is applicable for a going concern, without considering the event of amalgamation or demerger.
- Depreciation shall have to be apportioned between the predecessor and the successor in the ratio of number of days for which such assets were held for their business purpose and used by them.

Depreciation to be apportioned = [W.D.V. as on 1.4.2011 + New Purchases on 01.05.2011]

= ₹ (6,50,000 + 50,000) = ₹ 7,00,000 × 10% = ₹ 70,000

Apportionment of Depreciation and Allowable Depreciation

Assessee	No. of Days	Depreciation on Assets on the date of succession	Depreciation on Assets acquired after Succession	Total Depreciation for the Previous Year 2011-12
A Bros. (Sole-Proprietorship concern)	01.04.2011 to 30.9.2011 = 173 days	₹ 70,000 × 173/365 = ₹ 33,178	Nil	₹ 33,178
A Ltd. (Company)	21.09.2011 to 31.3.2012	₹ 70,000 × 192 × 365 ₹ 36,822	₹ 48,000 × 50% × 10% = ₹ 2,400 (Put to use < 180 days)	₹ 39,222

Illustration 9 : Amalgamation of Companies

P Ltd. was taken over by Q Ltd. with effect from 31.7.2011. This satisfies the conditions of Sec. 2(1B) of the Income Tax Act, 1961. From the following information, compute deductions admissible u/s 32 to P Ltd and Q Ltd. for the previous year 2011-12.

Assets	Rate of Depreciation	WDV in the hands of P Ltd (as on 01.04.2011)	Transfer Value to Q Ltd. (₹)
Building	10%	30,00,000	45,00,000
Plant & Machinery	15%	20,00,000	15,00,000
Motor Car	15%	8,00,000	6,00,000
Computers	60%	5,00,000	2,00,000
Furniture	10%	3,00,000	1,40,000

Solution :

- (1) Depreciation shall have to be calculated at the prescribed rates, as is applicable for a going concern, without considering the event of amalgamation or demerger.
- (2) Depreciation shall have to be apportioned between the predecessor and the successor in the ratio of number of days for which such assets were held for their business purpose and used by them.

Depreciation to be apportioned = [W.D.V. as on 1.4.2011 + New Purchases on 01.05.2011]

= ₹ (6,50,000 + 50,000) = ₹ 7,00,000 × 10% = ₹ 70,000

Depreciation Statement as per Income Tax Act, 1961

Particulars of Block of Assets	Rate Of Dept.	W.D.V as on 01.04.2010	Additional Actual Cost	Debenture	Net Value of Block	Depreciation for the Current Year	W.D.V. as on 31.3.2012
1	2	3	4	5	6	7	
Block I – Building	10%	30,00,000	Nil	Nil	30,00,000	3,00,000	27,00,000
Block – II Plant & Machinery	15%	20,00,000	Nil	Nil	20,00,000	3,00,000	17,00,000
Block – III Motor Car	15%	8,00,000	Nil	Nil	8,00,000	1,20,000	6,80,000
Block – IV Computers	60%	5,00,000	Nil	Nil	5,00,000	3,00,000	2,00,000
Block – V Furniture	10%	3,00,000	Nil	Nil	3,00,000	30,000	2,70,000
		56,00,000			56,00,000	10,50,000	45,50,000

TOTAL DEPRECIATION ADMISSIBLE ₹ 10,50,000

Apportionment of Depreciation and Allowable Depreciation

Assessee	No. of Days	Depreciation on Assets on the date of amalgamation	Depreciation on Assets acquired after amalgamation	Total Depreciation for the Previous Year 2010-11
P Ltd.	01.04.2011 to 31.7.2011 = 122 days	₹ 10,50,000 × 173/365 = ₹ 4,97,671	Nil	₹ 4,97,671
Q Ltd.	01.08.2011 to 31.3.2012 = 243 days	₹ 10,50,000 × 243 × 365 = ₹ 6,99,041	Nil	₹ 6,99,041

Depreciation : Personal Assets used in the Business

Illustration 10 :

Mr. Hari purchased a house property on 18.11.2007 for ₹15,00,000. Till 1.7.2011, the same was self-occupied for own residence. Thereafter, the said building was brought into use for the purpose of his profession. Determine the amount of depreciable admissible for the Assessment Year 2012-13, given rate of depreciation @ 10%.

Solution :

- (a) Property acquired by the assessee himself: As per Sec. 43(1), if a building/asset used for private purpose of the assessee is subsequently put to use for the purpose of business, the cost of acquisition shall be determined in the following manner:

Assessee : Mr. Hari
Previous Year : 2011-12
Assessment Year : 2012-13

	₹
Cost of acquisition of Residential House Property as on 18.11.2007	15,00,000
Less: Deemed depreciation for the Financial year 2007-08 @ 50% of 10% on ₹ 15,00,000 (since period of usage is less than 180 days)	75,000
WDV as on 01.04.2008	14,25,000
Less: Deemed Depreciation for Financial year 2008-09 @ 10% on ₹14,25,000	1,42,500
WDV as on 01.04.2009	12,82,500
Less: Deemed Depreciation for Financial year 2009-10 @ 10% on ₹12,82,500	1,28,250
WDV as on 01.04.2010	11,54,250
Less: Deemed Depreciation for Financial year 2010-11 @ 10% on ₹11,54,250	1,15,425
WDV as on 01.04.2011 = Actual cost for the purpose of charging depreciation	10,38,825
Less: Deemed Depreciation for Financial year 2011-12 @ 10% on ₹10,38,825	1,03,883
WDV as on 01.04.2012	9,34,942

Additional Depreciation :

Applicable	For assesses engaged in the business of manufacture or production of any article or thing
Assets eligible for additional depreciation	Any new plant or machinery acquired and installed after 31.3.2005
Assets not eligible for additional depreciation	(a) Ships and aircrafts; (b) Any machinery or plant which, before its installation by the assessee, was used either within or outside India by any other person, or (c) Any machinery or plant installed in any office premises or any residential accommodation, including accommodation in the nature of a guest house, or (d) Any office appliance or road transport vehicle, or (e) Any machinery or plant, the whole of which is allowed as deduction (whether by way of depreciation or otherwise) in computing the income chargeable under the head " profits and gains from business or profession" of any previous year
Rate of Additional Depreciation	20% of the Actual Cost of Plant or Machinery
Adjusted rate of additional depreciation	If the newly acquired asset is "put to use" for a period of less than 180 days during the previous year, in which it is acquired, the rate of additional depreciation shall be provided at 50% of the normal rate = $50\% \times 20\% = 10\%$

ASSET IS PARTLY USED FOR BUSINESS, PARTLY FOR PERSONAL PURPOSES [Sec. 38(2)]

If any asset is partly used for business and partly for personal purposes, depreciation u/s. 32(1)(ii) shall be restricted to a fair proportionate part thereof which the Assessing Officer may determine having regard to the user of such assets (building, machinery, plant or furniture) for the purposed of business or profession.

UNABSORBED DEPRECIATION [Sec. 32(2)]

Unabsorbed depreciation shall be treated as part of the current year depreciation such unabsorbed depreciation can be set off not only against income under "Profits and gains of Business or Profession" but also against income under any other head. Unabsorbed depreciation can be carried forward indefinitely and the business need not be continued in order to get the benefit of carry forward of unabsorbed depreciation.

INVESTMENT ALLOWANCE [Sec.32A]

In respect of a ship or an aircraft or machinery or plant specified in sub-section (2), which is owned by the assessee and is wholly used for the purposes of the business carried on by him, there shall, in accordance with and subject to the provisions of this section, be allowed a deduction, in respect of the previous year in which the ship or aircraft was acquired or the machinery or plant was installed or, if the ship, aircraft, machinery or plant is first put to use in the immediately succeeding previous year, then, in respect of that previous year, of a sum by way of investment allowance equal to twenty-five per cent of the actual cost of the ship, aircraft, machinery or plant to the assessee.

TEA/COFFEE/RUBBER DEVELOPMENT ACCOUNT [Sec. 33AB]

Sec.33AB Tea Development Account

Illustration 11 :

X Ltd., is a company engaged in the business of growing, manufacturing and selling of tea.

For the accounting year ended 31st March, 2011, its composite business profits, before an adjustment under section 33AB of the Income-tax Act, were ₹60 lakhs. In the year, it deposited ₹ 25 lakhs with NABARD.

The company has a business loss of ₹10 lakhs brought forward from the previous year.

The company withdrew in February, 2011 ₹20 lakhs from the deposit account to buy a non-depreciable asset for ₹18 lakhs and could not use the balance before the end of the accounting year. The withdrawal and the purchase were under a scheme approved by the Tea Board.

The non-depreciable asset was sold in November, 2011 for ₹29 lakhs.

Indicate clearly the tax consequences of the above transactions and the total income for the relevant years.

Computation of total income of X Ltd. for A.Y. 2011-12

Particulars	₹
Net profits before adjusting deduction u/s 33AB	60,00,000
Less: Deduction u/s 33AB	24,00,000
[Lower of (i) 40% of ₹60 lakhs = ₹24 lakhs; or (ii) actual amount deposited with NABARD = ₹25 lakhs]	
Profits after adjusting deduction u/s 33AB	36,00,000
As per Rule 8 of Income-tax Rules, 40% of this sum is subject to income-tax and the balance 60% is treated as agricultural income.	
Hence, the business income is 40% of ₹36 lakhs	14,40,000
Add: Non-utilisation of amount withdrawn: ₹ 2 lakhs [i.e. (₹20 lakhs – ₹18 lakhs)]	
40% is taxable as business income (the balance 60% is treated as agricultural income).	80,000
Business income	15,20,000
Less: Business loss brought forward from the previous year	10,00,000
Total Income	5,20,000

Computation of total income of X Ltd. for A.Y. 2012-13

Particulars	₹
Business income (See Note 2)	7,20,000
Capital gains (Short-term) (See Note 1)	11,00,000
Total Income	18,20,000

Note 1 - Computation of capital gains

Particulars	₹
Sale proceeds	29,00,000
Less: Cost of acquisition	18,00,000
Short term capital gains (since the period of holding is less than 36 months)	11,00,000

Note 2 - Computation of business income Since the asset is sold within 8 years, the cost of the asset i.e. ₹ 18 lakhs should be treated as income since the same has been allowed as deduction in the assessment year 2011-12.

However, out of this ₹18 lakhs, 60% would be agricultural income and the balance 40% i.e. ₹7.2 lakhs would be business income of P.Y. 2011-12. This is because deduction under section 33AB was allowed in P.Y. 2011-12 before disintegration of income into agricultural income and non-agricultural income.

The assessment must satisfy the following conditions :

- The assessee must be engaged in the business of tea, coffee or rubber plantation in India
- The amount must be deposited in a "Special Account".
- The deposit should be made within the specified time limit.
- The accounts should be duly audited.

Amount of Deduction :

Least of the followings :

- Amount Deposited
- 40% of the Profit of the Business before any adjustment u/s 33AB & Sec. 72.

SITE RESTORATION FUND [Sec. 33ABA]

The amount deposited in site restoration fund including interest thereon or 20% of profits, whichever is less, in case of an assessee carrying on business of prospecting for, or extraction or production of, petroleum or prospecting for, or extraction or production of, petroleum or natural gas or both in India. The accounts are required to be audited and furnish of such report in form 3AD is necessary to avail the deduction.

EXPENDITURE ON SCIENTIFIC RESEARCH [Sec. 35]

"Scientific Research" means any activities for the extension of knowledge in the field of natural or applied sciences including agriculture, animal husbandry and fisheries. [Sec. 43(4)]

Section	Particulars		Deduction
35(1) (i)	Revenue Expenditure related to the business — incurred for own business		
		– Current year	100%
		– Prior Period	100% upto 3 years prior to commencement

35(1) (ii)	Any sum paid to approved scientific Research Association or University or College or Institution	For undertaking Scientific research	125% of amount paid
35(1) (iia)	Any sum paid for scientific research, to a company, registered in India, having an object to carry out scientific research and development activities	For undertaking Scientific research	125% of amount paid
35(1) (iii)	Any sum paid to an approved University, College or other Institution	For research in social Science or statistical research	125% of amount paid
35 (2)	Capital expenditure incurred for own business (excluding cost of land)	related to the business Current year Prior Period	100% deduction 100% upto 3 years prior to commencement
35(2AA)	Any sum paid to National Laboratory or University or IIT or a specified person	For undertaking a programme approved by the prescribed authority	200% of amount paid
35(2AB)	In house research and development or Bio-technology in the business of manufacturer or production of any article or thing, not being an article or thing specified in list of Eleventh Schedule	Bio-technology or in-house research	200% of expense incurred

AMORTISATION OF TELECOM LICENCE FEES [Sec. 35ABB]

Amortization of Telecom Licence Fees [Sec 35ABB]

Expenditure incurred for obtaining licence to operate telecommunication services shall be allowed for deduction/ amortization, if the following conditions are satisfied:

- (i) Expenditure should be capital in nature;
- (ii) Expenditure should have been incurred for purpose of acquiring any right to operate telecommunication services;
- (iii) Payment should have been actually made to obtain a licence;
- (iv) Expenditure may be incurred either before commencement of business or at any time during the previous year.

Mode of calculating deduction :

- (i) If licence fees is actually paid before commencement of business
= Licence fees actually paid before commencement of business
No. of years from the previous year of commencement of business to the previous year in which licence expires
- (ii) If licence fees is paid after commencement of business
= Licence fees actually paid after commencement of business
No. of years from the previous year in which licence fee actually paid to the previous year in which licence expires

In case of transfer :

- (a) Calculate Unallowed amount = Actual cost of licence fee paid less amount of deduction already claimed u/s 35ABB



(b) For consideration received on transfer:

(i) If whole licence is transferred and net consideration is less than “Unallowed amount”

Business Expenditure = Unallowed amount less Net consideration

(ii) Where part of licence is transferred and net consideration is less than “Unallowed amount”

Amount of deduction = $\frac{\text{Unallowed amount less Net consideration}}{\text{Remaining period of licence}}$

(iii) Where whole or part of licence is transferred and net consideration is more than “Unallowed amount”

Net consideration more than Unallowed amount but less than Original Cost of licence	Business Income = Net Consideration less Unallowed amount
Net Consideration is more than Original Cost of licence and Un allowed amount	Business Income = Original cost of licence less Unallowed amount Capital Gain = Net Consideration less Original Cost of licence

The following table would explain the various situations

	A	B	C	D
Transfer of licence	Full	In Part	Full	In part
Licence period (years)	7	7	7	7
Acquisition cost	140	140	140	140
Deduction claimed so far (4 years)	80	80	80	80
Unamortised value	60	60	60	60
Sale price – current year	140	45	50	30
Amount remaining to be amortised		15		30
Amount deductible U/s.35ABB(3)			10	
Amount chargeable to tax as business income	80			
Amount to be amortised in remaining 3 years		5		10

Illustration 12 :

Free Call Ltd. obtained a telecom licence on 15.6.08 for a period of 8 years ending on 31.3.2016 against a fee of ₹30 crores to be paid in four instalments of ₹12 crores, ₹7 crores, ₹6 crores, ₹5 crores by June 2009, June 2010, June 2011 and June 2012 respectively. Explain how the payment for licence fee shall be dealt under the Income Tax Act, 1961.

Solution :

Assessee : Free Call Ltd.

Previous Year 2011-12

Assessment Year : 2012-13

- U/s 35ABB, expenditure incurred for the purpose of acquiring any right to operate telecommunication services is allowed equally as deduction throughout the unexpired life of the licence. Deduction shall be allowed **only for the actual payment made**.
- If only part payment is made, amortization is based on the amount paid and not on the basis of total consideration. For any further payments, deduction/amortization is allowed equally for the remaining unexpired useful life.
- Computation of amount of eligible deduction u/s 35 ABB:

Previous year	Amount paid (₹ Crores)	Unexpired Period of Licence on the date of actual payment	Amount of Deduction (₹ Crores)
2008-09	12.00	8 years	1.50
2009-10	7.00	7 years	$[1.50 + (7.00/7)] = 2.50$
2010-11	6.00	6 years	$[2.50 + (6.00/6)] = 3.50$
2011-12	5.00	5 years	$[3.50 + (5.00/5)] = 4.50$

Illustration 13 :

Hello International Ltd. incurs an expenditure of ₹ 240 crores for acquiring the right to operate telecommunication services for Assam & Sikkim. The payment was made in November 2009 and the licence to operate the services was valid for 15 years. In December 2010, the company transfers part of the licence, in respect of Assam, to Hi International Ltd. for a sum of ₹56 crores and continue to operate the licence in Sikkim. What is the deduction allowable u/s 35ABB to Hello International Ltd. for the Assessment Year 2012-13?

Solution :

Assessee: Hello International Ltd.

Previous Year : 2011-12

Assessment Year : 2012-13

- (a) u/s 35ABB, where part of the Telecom Licence is transferred and Net Consideration received on such transfer, is less than the expenditure remaining unallowed, the amount of deduction shall be computed as follows :

(i) Unallowed amount as on 01.04.2010	= Total Expenditure Less Deduction for Financial Year 2009-10 = ₹240 crores Less (₹240 crores/licence period of 15 years) = ₹240 crores less ₹16 crores = ₹224 crores.
(ii) Net Consideration received	= ₹60 crores
(iii) Remaining period of licence	= 14 years (including current previous year)
(iv) Deduction u/s 35 ABB	= ₹ (224 crores less 56 crores) / 14 years= ₹ 12 crores.

Illustration 14 :

Jammer International Ltd. incurs an expenditure of ₹300 crores for acquiring the right to operate telecommunication services for Orissa and Jharkhand. The payment was made in August 2010 and the licence to operate the services was valid for 12 years. In December 2011, the company transfers part of the licence, in respect of Orissa to Hammer International Ltd. for a sum of ₹280 crores and continue to operate the licence in Jharkhand . What is the deduction allowable u/s 35ABB to Jammer International Ltd. for the Assessment Year 2012-13?

Solution:

Assessee: Jammer International Ltd.

Previous Year : 2011-12

Assessment Year : 2012-13

- (a) u/s 35ABB, where part of the Telecom Licence is transferred and Net Consideration received on such transfer, is more than the expenditure remaining unallowed, the amount of deduction shall be computed as follows :

(i) Unallowed amount as on 01.04.2011	= Total Expenditure Less Deduction for Financial Year 2009-10 = ₹300 crores Less (₹300 crores / licence period of 12 years) = ₹300 crores less ₹25 crores= ₹275 crores.
(ii) Net Consideration received	= ₹280 crores
(iii) Remaining period of licence	= 11 years (including current previous year)
(iv) Deduction u/s 35 ABB	= ₹ (275 crores less 280 crores) / 11 years = ₹12 crores.



Sec. 35D Amortisation of Preliminary Expenses

Illustration 15 :

Sleepwell Ltd. is an existing Indian Company, which sets up a new industrial unit. It incurs the following expenditure in connection with the new unit:

	₹
Preparation of project report	4,00,000
Market survey	5,00,000
Legal and other charges for issue of additional capital required for the new unit	2,00,000
Total	11,00,000
The following further data is given:	
Cost of project	30,00,000
Capital employed in the new unit	40,00,000

What is the deduction admissible to the company under section 35D for Assessment Year 2012-13?

Solution:

The deduction admissible under section 35D is one-fifth of the expenditure incurred for the project. This works out to ₹ 2,20,000.

However, such expenditure should not exceed the following limits as prescribed in section (3):

- (a) 5% of cost of the project or
- (b) 5% of the capital employed in the new industrial undertaking (being a company) — whichever is higher.

In this case

- (a) 5% of the project cost is ₹ 1,50,000 and
- (b) 5% of the capital employed is ₹ 2,00,000.

Hence, the expenditure eligible for amortization under section 35D would be ₹ 2,00,000.

And the admissible deduction for the current assessment year is $2,00,000 \times 1/5 = ₹ 40,000$.

Illustration 16 :

Ms.Chitrakha, a retail trader of Kolkata furnishes the following Trading and Profit and Loss Account for the year ending 31st March, 2012 :

Trading and Profit and Loss Account for the year ended 31.03.2012

	₹		₹
To Opening stock	90,000	By Sales	12,11,500
To Purchases	10,04,000	By Income from UTI	2,400
To Gross Profit	3,06,000	By Other business receipts	6,100
		By Closing stock	1,80,000
	14,00,000		14,00,000
To Salary	60,000	By Gross profit b/d	3,06,000
To Rent and rates	36,000		
To Interest on loan	15,000		
To Depreciation	1,05,000		
To Printing & stationery	23,200		
To Postage & telegram	1,640		
To Loss on sale of shares (Short term)	8,100		
To Other general expenses	7,060		
To Net Profit	50,000		
	3,06,000		3,06,000

Additional Information :

- (i) It was found that some stocks were omitted to be included in both the Opening and Closing Stock, the values of which were

Opening stock	₹ 9,000
Closing stock	₹ 18,000

- (ii) Salary includes ₹10,000 paid to his brother, which is unreasonable to the extent of ₹2,000.
- (iii) The whole amount of printing and stationery was paid in cash.
- (iv) The depreciation provided in the Profit and Loss Account ₹ 1,05,000 was based on the following information :
The written down value of plant and machinery is ₹ 4,20,000. A new plant falling under the same Block of depreciation of 25% was bought on 1.7.2011 for ₹ 70,000. Two old plants were sold on 1.10.2011 for ₹ 50,000.
- (v) Rent and rates includes sales tax liability of ₹ 3,400 paid on 7.4.2011.
- (vi) Other business receipts include ₹ 2,200 received as refund of sales tax relating to 2009-10.
- (vii) Other general expenses include ₹ 2,000 paid as donation to a Public Charitable Trust.

You are required to advise Ms.Chitrlekha whether he can offer his business income for the A.Y. 2012-13.

Solution :

Computation of Income from Business

Assessee : Ms. Chitrlekha

A.Y : 2012-13.

	₹	₹
Net Profit as per profit and loss account		50,000
Add : Inadmissible expenses / losses		
Under valuation of closing stock	18,000	
Unreasonable salary paid to brother (section 40A(2))	2,000	
Printing and stationery paid in cash [Section 40A(3)] 100% of ₹23,200	43,200	
Depreciation (considered separately)	1,05,000	
Short term capital loss on shares	8,100	
Donation to public charitable trust	2,000	
		1,78,300
		2,28,300
Less : Deductions items:		
Under valuation of opening stock	9,000	
Income from UTI	2,400	
Refund of sales tax [Taxable u/s.41(1) – No adjustment necessary]	—	
		11,400
Business income before depreciation		2,16,900
Less : Depreciation (see note 1)		66,000
		1,50,900



Note 1

Calculation of depreciation

WDV of the block of plant & machinery as on the first day of previous year	4,20,000
Add : Cost of new plant & machinery	70,000
	<u>4,90,000</u>
Less : Sale proceeds of assets sold	50,000
WDV of the block of plant & machinery as on the last day of previous year	<u>4,40,000</u>
Depreciation @ 15%	<u>66,000</u>

Note : No additional depreciation is allowable as the assessee is not engaged in manufacture or production of any article.

Note 2

Since sales-tax liability has been paid before the due date of filing return of income under section 139(1), the same is deductible.

Illustration 17 :

Mukund is a person carrying on profession as film artist. His gross receipts from profession are as under :

Financial year	2009-2010	1,25,000
Financial year	2010-2011	1,60,000
Financial year	2011-2012	1,80,000

Is he required to maintain any books of account under Section 44AA of the Income-tax Act? If so, what are these books?

Answer :

Section 44AA requires every person carrying on any profession, notified by the Board of the Official Gazette (in addition to the professions already specified) to maintain such books of account and other documents as may enable the Assessing Officer to compute his total income in accordance with the provisions of the Income-tax Act. The CBDT has notified the profession of film artists as one such profession (S.O. No.17E/12-1-77). Hence section 44AA applies to Mukund.

Sub-section (3) of section 44AA authorizes the Board to prescribe by rules, the books of account and other documents (including inventories) to be kept and maintained under sub-section (1), the particulars to be contained therein etc. The prescribed rule is Rule 6F, under which every person carrying on the specified profession, including a film artist, is required to maintain the books of account and other documents specified in sub-Rule (2).

However, under the proviso to Sub-Rule (1), nothing contained therein shall apply in the case of a person, if his gross receipts do not exceed ₹ 1,50,000/- in any one of the three years, immediately preceding the previous year.

The significance of this rule is that if the gross receipts from profession do not exceed ₹ 1,50,000 in any one of the previous 3 years, he is not required to maintain the books of account specified in sub-rule (2) of Rule 6F. Since in one of the three previous years the gross receipts are below ₹ 1,50,000, the assessee is not required to maintain books of account and other documents as he is not governed by section 44AA.

Illustration 18 :

Discuss the tax implications of the following transactions in the case of a doctor running a nursing home :

	₹
(1) Amount paid to a scientific research association approved by the Central Government and run by a drug manufacturing company	20,000
(2) Amounts received from the employees of the nursing home as contributions towards provident fund for the month of March, 2012 paid to the PF Commissioner on 25 th April, 2012	25,000
(3) Repayment made in cash towards purchases of medicines	50,000
(4) Repayment of loan taken from a bank for doing a post-graduate course in medicine – instalment	50,000
Interest	10,000

Answer :

- (i). Under section 35(ii), 175% of the sums paid to scientific research association, which has as its object the undertaking of scientific research is deductible.

Deduction admissible = 20,000 × 175%

= ₹ 35,000.

- (ii) Under clause (x) of sub section 24 of section 2, any sum received by an assessee from his employees as contribution to any provident fund is deemed to be his income. Such income is deductible under section 36(1) (va) only if it is credited to the employees' account in the relevant fund by the due date.

Under Employees' Provident Fund Act, the due date for the payment of the contribution is the 15th of the month following the month for which the contribution is due. A grace period of 5 days is also allowed. Hence the payment of the employee's contribution for the P.F. Commissioner should have been made by 20th April. Since the payment has been made on 25th April, the deduction is not available.

- (iii) Under section 40A(3) payments made in cash exceeding ₹ 20,000 are not allowable in computing the income from business or profession. 20% of such expenditure is liable to be disallowed. Hence ₹ 10,000 will be disallowed. It is assumed that the case is not covered by the exceptions under Rule 6DD.
- (iv) Under section 80E, a deduction is admissible in the case of an individual towards any amount paid in the previous year by way of interest on loan taken from any financial institution for the purpose of pursuing his higher education. The purpose stated in the question is covered by the section. The deduction is allowable only towards payment of interest. The amount deductible under section 80-E would be ₹10,000.

EXPENDITURE ON ELIGIBLE PROJECTS/SCHEMES [Sec. 35AC]

Where an assessee incurs any expenditure by way of payment of any sum to a public sector company or a local authority or to an association or institution approved by the national committee for carrying out any eligible project or scheme it will be allowed as deduction. In order to avail the deduction under this section the assessee should furnish with return of income a certificate from the chartered accountant to that extent.

National committee can withdraw the approval granted by it to an association or institution on the ground that the project or scheme is not being carried out in accordance with all or any of the conditions subject to which approval was granted or the notification through which a project or scheme was notified after giving reasonable opportunity. The contribution or donation received by the company or authority or association or institution, as the case may be, or the deduction claimed by company in respect of any expenditure incurred directly on the eligible project or scheme, the approval for which is withdrawn by the national committee shall be deemed to be the income of the company or authority or association or institution as the case may be, of the year in which such approval or notification is withdrawn w.e.f. AY 2003-04 and shall be taxed at the maximum marginal rate of tax in force for that year.

**EXPENDITURE BY WAY OF PAYMENT TO ASSOCIATION AND INSTITUTION FOR CARRYING OUT RURAL DEVELOPMENT PROGRAMME [Sec. 35CCA]**

Where an assessee incurs any expenditure by way of payment of any sum- a) to an association or institution engaged in any programme of rural development, or b) to an association or institution which undertakes training of persons for implementing any programme of rural development or c) to National fund set up for rural development notified in this behalf by the Central Government or to the National urban poverty Eradication fund set up and notified by the Central Government he will be allowed a deduction of the amount of such expenditure incurred during the Previous Year.

Investment-linked tax incentive for specified business - cold chain facilities, warehousing facilities for storage of agricultural produce, and cross-country natural gas or crude or petroleum oil pipeline network for distribution, including storage facilities [Section 35AD, 28(vii) and 73A] [W.e.f. A.Y. 2010-11]

The Income tax Act provides for a number of profit-linked exemptions/deductions. Such benefits are inefficient, inequitable, impose higher compliance and administrative burden, result in revenue loss, increase litigations and lead to competitive demand for similar tax benefits. Further, these benefits also encourage diversion of profits from the taxed sector to the exempt/untaxed sector. However, investment-linked incentives are relatively less distortionary in their impact.

AMORTISATION OF CERTAIN PRELIMINARY EXPENSES [Sec. 35D]

The deduction is allowed under this section only in case of an Indian company or a person (other than company) resident in India. The deduction is in respect of the expenditure incurred after 31.3.1970 and expenditure may be of the type which was incurred —

- (i) before the commencement of the business, or
- (ii) after the commencement of his business, in connection with the extension of existing industrial unit.

The following expenses shall be eligible for deduction u/s 35D(2):

- (a) expenditure in connection with-
 - (i) preparation of feasibility report;
 - (ii) preparation of project report;
 - (iii) conducting market survey or any other survey necessary for the business of the assessee;
 - (iv) engineering services relating to the business of the assessee.
- (b) Legal charges for drafting any agreement between the assessee and any other person for any purpose relating to the setting up or conduct of the business of the assessee.
- (c) The following expenses in case of company assesseees :
 - (i) legal charges for drafting the Memorandum and Articles of Association of the company;
 - (ii) on printing of the Memorandum and Articles of association;
 - (iii) by way of fees for registering the company under the provision of the Companies Act, 1956;
 - (iv) in connection with the issue, for public subscription, of shares in or debentures of the company being underwriting commission, brokerage and charges for drafting, typing, printing and advertisement of the prospectus.
- (d) Such other item of expenditure (not being expenditure eligible for any allowance or deduction under any other provision of this Act) as may be prescribed.

Mode of Deduction:

Deduction of qualified amount is allowed in 5 equal instalments beginning with the Previous Year in which the business is commenced.

Amount of expenditure qualifying for deduction :-

The aggregate amount of expenditure referred to clause (a) to (d) above shall not exceed 5% cost of project if such expenditure incurred after 1.4.1998. But in case of an Indian company, 5% of the cost of the project or 5% of the capital employed at the option of the company.

“Capital employed” means the aggregate of issued capital debentures and long term borrowings (repayable during a period of not less than 7 years) as on the last day of relevant Previous Year. The qualifying amount of preliminary expenditure is allowed as deduction over a period of 5 years in equal installments.

In case of an Indian company under amalgamation/demerger, no deduction shall be allowed to amalgamating/demergered company for the Previous Year in which amalgamation/demerger takes place. Deduction is allowed to the amalgamated company/ resulting company in the same manner as allowable to amalgamating/demergered company. Audit of accounts is necessary for claiming deduction where accounts are not audited under any other law.

AMORTISATION OF EXPENDITURE IN CASE OF AMALGAMATION OR DEMERGER [Sec. 35DD]

Where an Indian company incurs any expenditure on or after 1.4.1999, wholly and exclusively for the purposes of amalgamation or demerger of an undertaking, the assessee company is allowed deduction in respect of such expenditure over a period of five years equally beginning with the Previous Year in which amalgamation or demerger takes place.

AMORTISATION OF EXPENDITURE INCURRED UNDER VOLUNTARY RETIREMENT SCHEME [Sec. 35DDA]

Where any expenditure is incurred by way of compensation to an employee under VRS in accordance with any scheme is allowed deduction over a period of 5 years equally from the year in which compensation is paid. W.e.f. Assessment Year 2001-02 inserted by the Finance Act, 2002 to provide that where an undertaking of an Indian company, entitled to deduction for amortisation of voluntary retirement expenses, is transferred before the expiry of the period specified to another Indian company in a scheme of amalgamation or demerger, the deduction shall continue to be available to the amalgamated company or the resulting company as if the amalgamation or demerger had not taken place.

In case of reorganisation of certain form of business where by a firm for a proprietary concern is succeeded by a company, the deduction shall continue to be available to the successor company. Deduction is not available to amalgamating company or demergered company or to the firm or proprietary concern, as the case may be, in the year of transfer.

Illustration 19 : Suppose the payment of voluntary retirement is made of X as under :

Previous year	Amount paid (₹)
2008-09	20,00,000
2009-10	12,00,000
2010-11	14,00,000
	46,00,000

In this case the deduction of expenses incurred under voluntary retirement scheme shall be allowed as under :

Assessment year 2009-10 : ₹ 4,00,000 (1/5th of ₹ 20,00,000) and balance ₹ 16,00,000 in 4 equal instalments in the next four assessment years i.e. assessment years 2009-10 to 2012-13.

Assessment year 2010-11 : ₹ 6,40,000 i.e. ₹ 4,00,000 on account of payment made in previous year 2007-08 and ₹ 2,40,000 (1/5th of ₹ 12,00,000 paid on previous year 2008-09).

Assessment year 2011-12 : ₹ 9,20,000 i.e. ₹ 6,40,000 (₹ 4,00,000 + ₹ 2,40,000 for payment made in previous year 2007-08 and 2008-09 respectively) and ₹ 2,80,000 on account of payment made in previous year 2009-10.

Assessment year 2012-13 : ₹ 9,24,000 (₹ 4,00,000 + ₹ 2,40,000 + ₹ 2,80,000)

Assessment year 2013-14 : ₹ 9,20,000 (₹ 4,00,000 + ₹ 2,40,000 + ₹ 2,80,000)

Assessment year 2014-15 : ₹ 5,20,000 (₹ 2,40,000 + ₹ 2,80,000)

Assessment year 2015-16 : ₹ 2,80,000

Total amount allowed in various assessment years ₹ 46,00,000.

**DEDUCTION FOR EXPENDITURE ON PROSPECTING etc. FOR CERTAIN MINERALS [Sec. 35E]**

Where an assessee being a Indian company or a person other than a company who is resident in India, is engaged in any operation relating to prospecting for, extraction or production of any mineral and incurs after 31.3.1970 any expenditure during the period of 5 years ending with the year of commencement of commercial production is allowed as deduction over a period of 10 years in equal installments.

Auditing of Accounts : The accounts of the assessee have got to be audited by a qualified chartered accountant and a copy of the audited report is to be sent as an accompaniment to the return of income. Companies and cooperative societies getting their accounts audited ordinarily need not get them audited specifically for this purpose.

Expenses amortised not deductible : Expenses which are included for amortisation will not be deducted while computing business profit or loss under any other section of this Act.

OTHER DEDUCTIONS [Sec. 36]

The deduction provided for in the following clauses shall be allowed in respect of the matters dealt with therein, in computing the income referred to in Sec. 28.

INSURANCE PREMIUM FOR STOCK AND STORES [Sec. 36(1)(i)]

The amount of any insurance premium paid in respect of insurance against risk of damage or destruction of stocks or stores used for the purpose of the Business or Profession.

PREMIUM PAID BY FEDERAL MILK COOPERATIVE SOCIETY [Sec. 36(1)(ia)]

A federal milk cooperative will be allowed deduction in respect of any premium paid by it towards an insurance policy in the life of cattle owned by a member of a primary cooperative society, which is engaged in supply of milk (raised by its members) to the federal milk cooperative society.

PREMIUM FOR EMPLOYEES' HEALTH INSURANCE [Sec. 36(1)(ib)]

The amount of any premium paid by any mode of payment other than cash by the assessee as an employer to effect or to keep in force an insurance on the health of his employees under a scheme in this behalf by the General Insurance Corporation of India and approved by the Central Government.

BONUS OR COMMISSION TO EMPLOYEES [Sec. 36(1)(ii)]

Any sum paid to an employee as bonus or commission for services rendered is deductible provided it would not otherwise be payable to him as profits or dividend, before due date subject to section 43B.

INTEREST ON BORROWED CAPITAL [Sec. 36(1)(iii)]

The amount of the interest paid in respect of capital borrowed for the purposes of the business or profession subject to section 43B.

CONTRIBUTION TOWARDS RECOGNISED PROVIDENT FUND OR AN APPROVED SUPERANNUATION FUND [Sec. 36(1)(iv)]

Any sum paid by the assessee as an employer by way of contribution to a recognized provident fund or an approved superannuation fund subject to limits prescribed in this regard in Sec. 43B.

CONTRIBUTION TOWARDS AN APPROVED GRATUITY FUND [Sec. 36(1)(v)]

Any sum actually paid by an employer by way of contribution towards an approved gratuity fund created by him for the exclusive benefit of his employees under an irrecoverable trust subject to Sec. 43B.

CONTRIBUTIONS RECEIVED FROM EMPLOYEES TO A WELFARE OF THE EMPLOYEES [Sec. 36(1)(va)]

Deductions in respect of any sum received by the assessee a contribution from his employees towards provident fund or any other welfare fund of such employees is allowed only if such sum is credited by [the tax payer] to

the employees accounts in the relevant funds on or before due date. If payment is not made within the due date such contribution should be treated as income of the assessee.

However, deduction will be allowed in respect of any such sum received as stated above only if such sum is credited by the assessee to the employee's account in relevant fund on or before the due date, i.e. the date by which the assessee is required as an employer to credit such contribution to the employee's account under the provisions of any law or term of contract of service or otherwise.

DEDUCTION IN RESPECT OF ANIMALS USED FOR BUSINESS WHICH HAVE DIED OR BECOME PERMANENTLY USELESS [Sec. 36(1)(vi)]

In respect of animals used for the purpose of Business or Profession (but not stock in trade) who have died or become permanently useless, the difference between the actual cost to the assessee of the animals and the amount, if any, realised in respect of carcasses or animals, will be allowed as a deduction.

BAD DEBTS [Sec. 36(1)(vii)]

Any bad debt or part thereof which is written off as irrecoverable in the accounts of the assessee for the Previous Year will be allowed as deduction if—

- (i) the debt is incidental to business,
- (ii) it should have been taken into account in computing income of the assessee, or it should represent money lent in the ordinary course of banking or money lending business,
- (iii) it should be written off in the books of account
- (iv) the business in respect of which the debt is incurred should be continued during, the Previous Year.

The successor of a business is entitled to claim deduction in respect of debt created by the predecessor CIT Vs. T. Veerabhadra Rao, K. Koteswara Rao & Co. 155 ITR 152.

PROVISION FOR BAD AND DOUBTFUL DEBTS MADE BY [Sec. 36(1)(viiia)] :-

- (i) Schedule bank (not incorporated outside India) or non-schedule bank or a co-operative bank other than a primary agricultural credit society or a primary co-operative agricultural and rural development bank, upto 7.5% of its total income and an addition at 10% average advances made by the rural branches of such bank. Option has also been given to bank to claim deduction in respect of any provision for doubtful or loss of assets as per RBI guidelines, upto a maximum of 5% of such assets at the end of the relevant Previous Year for the AY 2000-01 to 2002-03 and upto 10% of such assets for AY 2003-04 and 2004-05.
- (ii) A bank incorporated outside India upto 5% of its total income.
- (iii) A Public Financial Institution on a State Financial Corporation or a state industrial investment corporation, upto 5% of its total income. Option is also given to Financial Institution/Corporation to claim deduction in respect of any provision for doubtful or loss assets as per RBI guidelines, upto a maximum of 10% of such assets at the end of the Previous Year relevant to Assessment Year 2003-04 or 2004-05.

Total income for this purpose means income computed before making any deduction under chapter VIA.

SPECIAL RESERVE CREATED AND MAINTAINED BY A FINANCIAL CORPORATION [Sec.36(1)(viii)]

Deduction under this section is allowed in respect of any special reserve created and maintained by :

- (a) to a financial corporation which is engaged in providing long time finance for industrial or agricultural or development in India or for development for infrastructure facility in India; or
- (b) by a public company formed and registered in India with the main objective of carrying on the business of providing long time finance for construction of purchase of houses in India for residential purposes.

The deduction under this section shall be an amount transferred to reserve account or an amount not exceeding 20 % of the profits derived from such business which ever is less. If the amount of reserve is more than twice the paid up share capital and general reserve, the excess amount is not deducted.

Special deduction under section 36(1)(viii) allowed to National Housing Bank of an amount not exceeding 20% of the profits subject to creation of a reserve [Section 36(1)(1)(viii)][W.e.f. A.Y. 2010-11]



Section 36(l)(viii) provides special deduction to financial corporations and banking companies of an amount not exceeding 20% of the profits subject to creation of a reserve.

National Housing Bank (NHB) is wholly owned by Reserve Bank of India and is engaged in promotion and regulation of housing finance institutions in the country. It provides re-financing support to housing finance institutions, banks, ARDBs, RRBs, etc., for the development of housing in India. It also undertakes financing of slum projects, rural housing projects, housing projects for EWS and LIG categories, etc. NHB is also a notified financial corporation under section 4A of the Companies Act.

A view has been expressed that NHB is not entitled to the benefits of section 36(l)(v/ii) on the ground that it is not engaged in the long-term financing for construction or purchase of houses in India for residential purpose. The amendment has been made in clause (b) of Explanation to section 36(l)(v/ii) to provide that corporations engaged in providing long-term finance (including re-financing) for development of housing in India will be eligible for the benefit under section 36(l)(viii).

EXPENDITURE INCURRED BY COMPANY FOR PROMOTING FAMILY PLANNING AMONGST ITS EMPLOYEES [Sec. 36(1)(ix)]

The company assessee is entitled to claim deduction in respect of bonafide revenue expenditure incurred by it in a Previous Year for the purposes of promoting family planning amongst its employees. In case of expenditure of a capital nature, the deduction is allowed in 5 equal yearly installments commencing from the previous year in which such expenditure is incurred.

The capital expenditure under this section is governed by the same conditions as are applicable to capital expenditure for scientific research. The unabsorbed expenditure under this section can be carried forward and set off in the following years like unabsorbed depreciation allowance.

Commodities Transaction Tax not operationalised (Section 36(1)(xvi)) [W.r.e.f. A.Y. 2009-10]

The provisions for levy of Commodities Transaction Tax were introduced by Chapter VII of Finance Act, 2008. However, the levy has not yet been operationalised. In view of the recommendations of the Prime Minister's Economic Advisory Council, a new section 121A in Chapter VII of Finance Act, 2008 has been inserted to provide that the Chapter relating to levy of Commodities Transaction Tax shall not apply on or after 1-4-2009.

The Act has made it consequential amendment in clause (xvi) in sub-section (1) of section 36 of the Income-tax Act by omitting the said clause, where CTT was allowable as deduction.

GENERAL DEDUCTIONS [Sec. 37]

Any expenditure (not being expenditure of the nature described in sec. 30 to 36), and not being in the nature of capital expenditure or personal expenses of the assessee paid out or expended wholly and exclusively for the purposes of the business profession shall be allowed in computing the income chargeable under the head "Profits and gains of Business or Profession"- Sec. 37(1).

The conditions to be fulfilled for general deductions u/s. 37 are as follows—

- (i) It should be in respect of a business carried on by an assessee;
- (ii) It should have been paid out or expended wholly and exclusively for the purpose of the business;
- (iii) It must have been incurred during the Previous Year; and
- (iv) It should not be in the nature of capital expenditure or personal expenses of the assessee.

Thus expenses incurred on the occasion of Dewali or Mahurat subject to being satisfied that the expenses are not expenses of a personal, social or religious nature- allowed deduction u/s.37.

Loss through embezzlement by an employee or recurring expenses incurred on imparting basic training to apprentices under the Apprentices Act, 1961 are general deductions u/s. 37.

Any expenditure incurred by an assessee for any purpose which is an offence or which is prohibited by law shall not be deemed to have been incurred for the purpose of business or profession and no deduction or allowance shall be made in respect of such expenditure [Explanation to Sec. 37(1)].

ADVERTISEMENT EXPENDITURE [Sec. 37(2B)]

No allowance shall be made in respect of expenditure incurred by an assessee on advertisement in any Souvenir, Brochure, Pamphlet or the like published by a political party.

INADMISSIBLE EXPENDITURE [Sec. 40, 40A, 43B]

SECTION 40(a)

- Interest, salary, royalty, fees for beneficial services or any other sum payable outside India is not deductible unless tax is deducted at source or tax is paid.
- Income Tax and Wealth Tax are not deductible.
- Any tax paid by the employer on the perquisites not provided by way of monetary payment is not deductible in computing business income of the employer w.e.f. Assessment Year 2003-04.

DISALLOWANCE IN THE CASE OF PARTNERSHIP FIRMS (INCLUDING LIMITED LIABILITY PARTNERSHIP) [Sec. 40(b)] [w.e.f. A.Y. 2010-11]

(i) Interest to a partner by a firm is not deductible unless the following conditions are fulfilled:

1. It should be authorised by the partnership deed.
2. It should relate to a period falling after the date of the Partnership deed.
3. It should not exceed 18% p.a. (12% p.a. w.e.f. 1.6.2002) simple rate of interest.

Explanation 1 : If a person is a partner in his representative capacity in the firm and if he receives interest in his individual capacity from the firm such interest should not be disallowed.

Explanation 2 : If a person who is a partner in his individual capacity receives interest for and on behalf of some one else from the firm in which he is a partner such interest should not be disallowed.

(ii) Any amount paid by way of salary, bonus, commission or remuneration by a firm to a partner is not deductible in the computation of income of the firm unless the following conditions are fulfilled :

1. It should be authorised by partnership deed.
2. It should relate to a period falling after the date of the partnership deed.
3. It should be within the prescribed limits as follows :—

The Act has made upward revision of the existing limits of the remuneration. Further, uniform limits have been prescribed for both professional and non-professional firms for simplicity and administrative case. The revised limits are as under :

(a) On the first ₹ 3,00,000 of the book-profit or in case of a loss	₹ 1,50,000 or at the rate of 90% of the book-profit, whichever is more;
(b) On the balance of the book-profit	At the rate of 60%.

4. It should be paid to a working partner.

Explanation 3 : “Book profit” means the net profit, as shown in 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 all the partners of the firm if such amount has been debited while computing the net profit.

Explanation 4 : “Working partner” means an individual who is actively engaged in conducting the affairs of the Business or Profession of the firm of which he is a partner.

CBDT issued circular no. 739 dt. 25.3.96 stating that disallowance of salary to partners shall be made in the case of a firm if the partnership deed does not specify the amount of remuneration payable to each individual working partner or it does not lay down the manner of quantifying such remuneration.

DISALLOWANCE IN THE CASE OF ASSOCIATION OF PERSONS AND BODY OF INDIVIDUALS [Sec. 40(ba)]

Any payment by way of interest, salary, bonus, commission or remuneration paid by an association of persons or body of individuals to any of its members shall be disallowed.

Explanation 1 : If the member who received interest from the AOP or BOI also pays interest to the AOP or BOI during the same Previous Year only the net excess interest paid by the AOP to such member should be disallowed.



Explanation 2 : If a person is a member in his representative capacity in the AOP or BOI and if he received interest in his individual capacity from the AOP or BOI such interest should not be disallowed.

Explanation 3 : If a person who is a member in his individual capacity received interest for and on behalf of some one else from the AOP or BOI in which he is a member such interest should not be disallowed.

SECTION 40A(1)

Expenses or payment as provided in subsection (2), (3), (7) and (9) of Section 40A are not deductible.

SECTION 40A(2)

Where an assessee incurs any expenditure, in respect of which payment has been made or is to be made to certain specified persons and in the opinion of Assessing Officer such expenditure is excessive or unreasonable having regard to the fair market value of the goods, services or facilities for which the payment is made, then so much of expenditure which is considered by the Assessing Officer to be excessive or unreasonable, shall not be allowed as deduction.

Assessee	Specified persons
(i) Individual	(a) any relative (i.e., spouse, any brother, sister, lineal ascendant descendant) of such individual; (b) any person in whose business or profession the assessee (i.e. individual) himself or his relative has substantial interest.
(ii) Company, firm, AOP or HUF	(a) any director of the company, partner of the firm, or member of the association, or family, or any relative of such director, partner or member; (b) any person in whose Business or Profession the assessee or director, partner or member of the assessee or any relative of such person has a substantial interest.
(iii) All assesseees	(a) any individual who has substantial interest in the Business or Profession of the assessee; (b) a company, firm, AOP or HUF having a substantial interest in Business or Profession of the assessee or any director, partner or member of any such person or any relative of any.

DISALLOWANCE OF CASH EXPENDITURE EXCEEDING ₹ 20,000 [Sec. 40A(3), RULE 6DD]

Where the assessee incurs any expenditure incurred over ₹ 20,000 otherwise than by account payee cheque drawn on a bank or account payee bank draft, 100% deduction will be disallowed in respect of such expenditure.

Enhancement of limit for disallowance of expenditure made otherwise than by an account payee cheque or account payee bank draft for plying, hiring or leasing goods carriages in the case of transporters to ₹ 35,000 from the existing limit of ₹ 20,000 (Section 40A(3) and (3A) (applicable to transactions effected on or after 1-10-2009)

Under the existing provisions of the Income-tax Act, where an assessee incurs any expenditure, in respect of which payment in excess of ₹ 20,000 is made otherwise than by an account payee cheque or account payee bank draft, such expenditure is not allowed as a deduction. Given the special circumstances of transport operators for incurring expenditure on long haul journeys for plying, hiring or leasing goods carriages, the Act has inserted proviso 2 to section 40A(3) and (3A) in order to raise the limit of payment to such transport operators otherwise than by an account payee cheque or account payee bank draft to ₹ 35,000 from the existing limit of ₹ 20,000.

The existing limit for other categories of payments will remain at ₹ 20,000 subject to the exceptions declared in Rule 6DD of the Income-tax Rules.

Exceptions under rule 6DD

- Payments made to banks, including cooperative bank or land mortgage bank, Life Insurance Corporation and financial institution like IDBI, UTI, Industrial Development Corporations and State Financial Corporations, primary agricultural credit society.
- Payments made to Government, where such payment is required to be made in legal tender e.g. payment of sales-tax, customs duty, excise duty, etc.
- Payments under contracts entered into before 1.4.1969.

- (d) Payments made by way of any Letter of Credit, telegraphic transfer, transfer from one bank account to another, or through Bill of Exchange payable to a bank.
- (e) Where the payment is made by way of adjustment against the amount of any liability incurred by the payee for any goods supplied or services rendered by the assessee to such payee.
- (f) Payment for purchase of
 - (i) agricultural or forest produce,
 - (ii) the produce of animal husbandry (including hides and skins), dairy or poultry farming,
 - (iii) fish or fish-products, or
 - (iv) products of horticulture, or apiculture if the payment is made to the cultivator, grower or producer of such articles, produce or products.
- (g) Payment made for purchase of products manufactured or processed without the aid of power in a cottage industry, if the payment is made to the producer of such products.
- (h) Where the payment is made in a village or town, which is not served by any bank, to any person who ordinarily resides or is carrying on any business, profession or vocation in any village or town.
- (i) Payment by way of gratuity, retrenchment compensation or similar terminal benefits made to an employee or his legal heirs, if the income under the head salary of the employee does not exceed ₹ 7500 for the current year as well as for the immediately preceding Previous Year.
- (j) Payment made by way of salary to its employees after deducting the income-tax from the salary, when such an employee is temporarily posted for a continuous period of fifteen days or more in a place other than his normal place of duty or on a ship and the employee does not maintain any account in any bank at such place.
- (k) Where the payment is required to be made on a day on which the banks were closed, either on account of holiday or strike.
- (l) Payments made by any person to his agent who is required to make payments in cash for goods or services on behalf of such person.
- (m) Where the payment is made by an authorised dealer or a money changer against purchase of foreign currency or travellers cheques in the normal course of his business. [Notification No. 11476, dated 6.9.2000 applicable retrospectively from 25.7.1995]

PROVISION FOR GRATUITY [Sec. 40A(7)]

No deduction shall be allowed in respect of any provision made by the assessee for the payment of gratuity to his employees on their retirement or on termination of their employment for any reason. However, any provision made by the assessee for the purpose of payment of any contribution towards an approved gratuity fund or for the purpose of payment of any gratuity which has become payable during the Previous Year shall be allowed as deduction.

NON STATUTORY/UNRECOGNISED WELFARE FUND CONTRIBUTIONS [Sec. 40A(9)]

Any contribution made by the assessee to unrecognised or non-statutory welfare fund accounts is not deductible.

Special provision for computing deductions in the case of business reorganization of co-operative banks [Sec. 44DB]

After section 44DA of the Income-tax Act, the following sections shall be inserted with effect from the 1st day of April, 2008, namely :—

44DB. Special provision for computing deductions in the case of business reorganization of co-operative banks.— (1) The deduction under section 32, section 35D, section 35DD or section 35DDA shall, in a case where business reorganization of a co-operative bank has taken place during the financial year, be allowed in accordance with the provisions of this section.



(2) The amount of deduction allowable to the predecessor co-operative bank under section 32, section 35D, section 35DD or section 35DDA shall be determined in accordance with the formula—

		B
A	×	C

where A = the amount of deduction allowable to the predecessor co-operative bank if the business reorganisation had not taken place;
 B = the number of days comprised in the period beginning with the 1st day of the financial year and ending on the day immediately preceding the date of business reorganisation; and
 C = the total number of days in the financial year in which the business reorganisation has taken place.

(3) The amount of deduction allowable to the successor co-operative bank under section 32, section 35D, section 35DD or section 35DDA shall be determined in accordance with the formula—

		B
A	×	C

where A = the amount of deduction allowable to the predecessor co-operative bank if the business reorganisation had not taken place;
 B = the number of days comprised in the period beginning with the date of business reorganisation and ending on the last day of the financial year; and
 C = the total number of days in the financial year in which the business reorganisation section is transferred before the expiry of the period specified therein to a successor co-operative bank on account of business reorganisation, apply to the successor co-operative bank in the financial years subsequent to the year of business reorganisation as they would have applied to the predecessor co-operative bank, as if the business reorganisation had not taken place.

DEEMED PROFIT/DEEMED INCOME [Sec 41(1)]

Where deduction has been made in respect of loss, expenditure or trading liability for any year and subsequently the assessee or successor of the business has obtained any amount in respect of such loss expenditure or some benefit in respect of such trading liability by way of remission or cessation thereof, the amount obtained or the value of benefit accrued shall be deemed to be income.

The provisions are applicable even to the successor who receives the amount/benefit.

The 'successor in business', for this purpose, means—

- Where there has been an amalgamation of a company with another company, the amalgamated company;
- Where any person is succeeded by another person in carrying on the Business or Profession, such other person;
- Where a firm carrying on a Business or Profession is succeeded by another firm, such other firm.
- Where there has been a demerger, the resulting company.

If there is a remission or cessation of a trading liability which was earlier allowed as deduction, it is chargeable to tax. Even if the remission or cessation is effected by a unilateral Act of writing off of such liability by the assessee, the amount so written off is chargeable to tax.

The above mentioned sub-section covers loss, expenditure and trading liability.e.g.

- If stock is destroyed by fire and allowed as trading loss but later insurance compensation is received, the same is assessable u/s. 41(1).
- If credit purchase of raw material is made and claimed as deduction but later, a lesser amount is settled to the supplier creditor, the benefit accruing on remission of the trading liability will be deemed as income u/s. 41(1).

SECTION 41(2)

In the case of an undertaking engaged in the generation or generation and distribution of power, option is available to claim depreciation on straight line method with reference to each individual asset. If such option is exercised, block of asset concept does not apply. In the case of such an assessee, where any building, machinery, plant or furniture is transferred for a consideration which is more than the depreciated value, the surplus to the extent of depreciation already allowed shall be assessed as business income. This is normally described as 'balancing charge'.

SECTION 41(3)

Any amount realised on transfer of an asset used for scientific research is taxable as business income to the extent of deduction allowed u/s. 35 in the year in which the transfer takes place.

SECTION 41(4)

Any amount recovered by the assessee against bad debt earlier allowed as deduction shall be taxed as income in the year in which it is received.

SECTION 41(4A)

Under sec. 36(1)(viii) any special reserve created and maintained by a financial corporation or public company specified there under qualifies for deduction subject to the limit prescribed. Sub-section (4A) is introduced in sec. 41 to make it clear that where a deduction has been so allowed, any amount subsequently withdrawn from such special reserve shall be deemed to be the profits of the year of such withdrawal and shall be charged to tax accordingly. The chargeability applies even if the business is no longer in existence during the relevant Previous Year.

SECTION 41(5)

In the case of an assessee who is chargeable to tax in respect of any amount deemed as profit u/s. 41 relating to a discontinued business, any loss incurred in the year in which the business was discontinued shall be allowed to be set off against such profit and only the balance, if any, shall be taxed.

SECTION 176(3A)

Where any business is discontinued in any year, any sum received after discontinuance shall be deemed to be the income of the recipient and 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.

SECTION 176(4)

Where any profession is discontinued in any year on account of the cessation of the profession by, or the retirement or death of, the person carrying on the profession, any sum received after the discontinuance shall be deemed to be the income of the recipient and charged to tax accordingly in the year of receipt, if such sum would have been included in the total income of the aforesaid person had in been received before such discontinuance.

CASH CREDITS [Sec. 68]

Where any sum is found credited in the books of an assessee, maintained for any Previous Year, and the assessee offers no explanation about the nature and source thereof or the explanation offered by him is not, in the opinion of the Assessing Officer, satisfactory, the sum so credited may be charged to income-tax as the income of the assessee of that Previous Year.

UNEXPLAINED INVESTMENTS [Sec. 69]

Where in the financial year immediately preceding the Assessment Year, the assessee has made investments which are not recorded in the books of account, if any, maintained by him for any source of income and the assessee offers no explanation about the nature and source of the investments or the explanation offered by him is not, in the opinion of the Assessing Officer, satisfactory, the value of the investments may be deemed to be the income of the assessee of such financial year.

**UNEXPLAINED MONEY ETC. [Sec. 69A]**

Where in any financial year, the assessee is found to be the owner of any money, bullion, jewellery or other valuable article and such money, bullion, jewellery or valuable article is not recorded in the accounts, if any maintained by him for any source of income, and the assessee offers no explanation about the nature and source of acquisition of the money, bullion, jewellery or other valuable article, or the explanation offered by him is not, in the opinion of the Assessing Officer, satisfactory, the money and the value of the bullion, jewellery or other valuable articles may be deemed to be the income of the assessee for such Financial Year.

INVESTMENTS, ETC. NOT FULLY DISCLOSED IN BOOKS OF ACCOUNT [Sec. 69B]

Where in any Financial Year, the assessee has made investments or is found to be the owner of any bullion, jewellery or other valuable article, and the Assessing Officer finds that the amount expended on making such investments or in acquiring such bullion, jewellery or other valuable article exceeds the amount recorded in his behalf in the books of account maintained by the assessee for any source of income and the assessee offers no explanation about such excess amount or the explanation offered by him is not, in the opinion of the Assessing Officer, satisfactory, the excess amount may be deemed to be the income of the assessee for such Financial Year.

UNEXPLAINED EXPENDITURE [Sec. 69C]

Where in any Financial Year, an assessee has incurred any expenditure and he offers no explanation about the source of such expenditure or part thereof, or the explanation, if any, offered by him is not, in the opinion of the Assessing Officer, satisfactory, the amount covered by such expenditure or part thereof, as the case may be, may be deemed to be the income of the assessee for such Financial Year.

Further, notwithstanding anything contained in any other provision of the Income Tax Act, such unexplained expenditure which is deemed to be the income of the assessee, shall not be allowed as a deduction under any head of income.

UNEXPLAINED AMOUNT BORROWED OR REPAID ON HUNDI [Sec. 69D]

Where any amount is borrowed on a hundi from, or any amount due thereon is repaid to, any person otherwise than through an account payee cheque drawn on a bank, the amount so borrowed or repaid shall be deemed to be the income of the person borrowing or repaying the amount aforesaid for the Previous Year, in which the amount was borrowed or repaid, as the case may be, provided that, if in any case any amount borrowed on a hundi has been deemed under the provisions of this Section to be the income of any person, such person shall not be liable to be assessed again in respect of such amount under the provisions of this Section on repayment of such amount.

Explanation : For the purposes of the Section, the amount repaid shall include the amount of interest paid on the amount borrowed.

EXCHANGE RATE FLUCTUATION [Sec. 43A]

Where an assessee acquires an asset from abroad and in consequence of the variation in exchange rate, the liability of the assessee in terms of payment towards the acquisition of that asset increases or decreases, then the actual cost of that asset shall be increased or decreased accordingly. The effect of exchange rate fluctuation shall be taken into consideration for the purpose of deduction u/s. 32, 35, 35A, 36(1)(ix) and for the purpose of computation of capital gains u/s. 48 or u/s. 50 as the case may be.

The increase or decrease in liability due to exchange rate fluctuation shall be taken into account at the time of making payment also.

SECTION 43B

Certain expenses are allowed only on payment basis within a stipulated time period irrespective of method of accounting and the evidence of such payment is furnished alongwith the return of income.

	Nature of Expense	Stipulated time period
1.	Any sum payable by way of tax, duty, cess or fee, by whatever name called, under any law for the time being in force.	Due amount should be paid on or before the due date of furnishing the return of income u/s. 139(1) in respect of the Previous Year.
2.	Any sum payable to an employee as bonus or commission for services rendered.	In which the liability to pay such sum was incurred and proof of payment should be attached alongwith the return of income.
3.	Any sum payable by the assessee as interest on any loan or borrowing from any public financial institution or State Financial Corporation or State Industrial Investment Corporation like IDBI, IFCI, UPSIDC, Delhi Financial Corporation, etc. in accordance with the terms and conditions of the agreement governing such loan or borrowing.	However, in cases (1) to (5), if the payment of outstanding liability is made after the due date, deduction can be claimed in the year of payment.
4.	Any sum payable by the assessee as interest on any term loan from a scheduled bank in accordance with the terms and conditions of the agreement governing such loan.	-do-
5.	Any sum payable by the assessee as an employer in lieu of any leave at the credit of his employee (inserted w.e.f. AY 2002-03)	However, if the deduction has already been allowed on due basis before this amendment, the same will not be allowed again when the sum is actually paid.
6.	Any sum payable by the assessee as an employer by way of contribution to any provident fund of superannuation fund or gratuity fund or any other fund for the welfare of employees.	Payments should be made in cash or by issue of a cheque or draft, or by any other mode on or before the due date by which the employer is required to credit an employee's contribution to the employee's account in the relevant fund under the respective Act, rule, order or notification. Where the payment has been made otherwise than in cash, the sum should be realised within fifteen days from the relevant due date

COST OF ACQUISITION OF CERTAIN ASSETS [Sec. 43C]

	Mode of acquisition	Cost of acquisition
1)	Amalgamation	(a) Cost to the amalgamating company (b) Cost of improvement (c) Expenses incurred for transfer
2)	Gift	(a) Cost to the donor, (b) Cost of improvement (c) Expenses incurred for accepting the gift and the gift tax paid by the donor
3)	Partition of HUF	(a) Cost to the HUF (b) Cost of improvement (c) Expenses incurred for partition.
4)	Will	(a) Cost to the previous owner (b) Cost of improvement (c) Expenses incurred for probating the will
5)	Irrevocable trust	(a) Cost to the previous owner (b) Cost of improvement (c) Expenses incurred for establishing the trust.



SPECIAL PROVISIONS FOR DEDUCTION IN CASE OF TRADE, PROFESSIONAL OR SIMILAR ASSOCIATION [Sec.44A]

Amount received from members of trade, professional or similar associations by way of subscription or membership fee falls short of the expenditure incurred, such deficit will be allowed as deduction in computing the income under the head "Profits and gains of Business or Profession". If there is no income under that head or if the income under that head is inadequate to absorb the deficit, it can be set off against the income of the association computed under any other head of income.

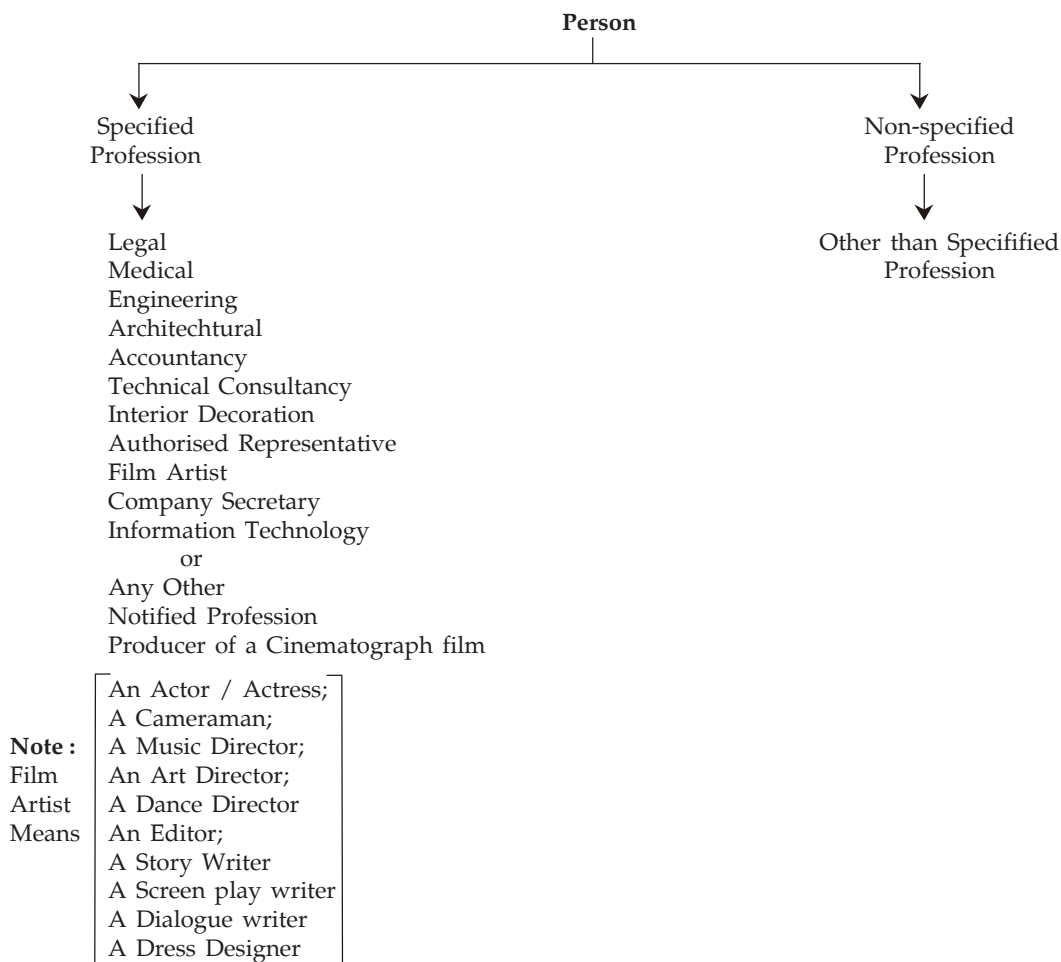
In any case any loss or allowance brought forward from earlier assessment year, the deduction permissible under this provision cannot exceed 50% of the total income for that previous year computed before allowing this deduction.

Sec, 44 is applicable only to the trade, professional or similar association the income of which or any part thereof is not distributed to its members except as grants to any association or institution affiliated to it.

Excess over expenditure received by a club from facilities extended to members as part of advantages attached to such membership shall not be chargeable to tax on the principle of mutuality- CIT vs. Bankipur Club Ltd. 226 ITR 97

COMPULSORY MAINTENANCE OF ACCOUNTS [Sec. 44AA, RULE 6F]

Applicability of this section depends on the type of activity carried on by the person. For this purpose. Persons are classified as follows :-



Requirement of Compulsory maintenance of Books of Account :

Catagory	Classification	Condition
A	<p>"Specified Person"</p> <p>↓</p> <p>Not Required to Maintain any Books of Account.</p>	<p>Gross Receipts \leq 1,50,000 in any of the three years immediately preceeding the previous year</p> <p>If newly set up in the previous year, then his Gross total receipts in the protection for that year are not likely to exceed the said amount</p>
B	<p>"Specified Person"</p> <p>↓</p> <p>Required to maintain such Books of Account as prescribed in Rule 6F.</p>	<p>Gross Receipts \geq 1,50,000 in all the three years immediately preceeding the previous year</p> <p>If newly set up in the previous year, then his Gross total receipts in the protection for that year are not likely to exceed the said amount</p>
C	<p>"Non-Specified Person"</p> <p>↓</p> <p>Not Required to Maintain any Books of Account</p>	<p>Income from such Business or Profession \leq 1,20,000 or total sale or turnover or Gross receipts there of are less than ₹ 10,00,000 (utpto A.Y. 2010-11) + ₹ 15,00,000 (for A.Y. 2011-12), as applicable in all the three years immediately preceeding the previous year</p> <p>If newly set up in the previous year, then his Gross total receipts in the protection for that year are not likely to exceed the said amount</p>
D	<p>"Non-Specified Person"</p> <p>↓</p> <p>Required to maintain such Books of Account as prescribed in Rule 6F.</p> <p>This category includes an assessee covered u/s 44AD, 44AE, 44BB, 44BBB</p>	<p>Income from such Business or Profession \geq 1,20,000 or total sale or turnover or Gross receipts there of are less than ₹ 10,00,000 (utpto A.Y. 2010-11) + ₹ 15,00,000 (for A.Y. 2011-12), as applicable in all the three years immediately preceeding the previous year</p> <p>If newly set up in the previous year, then his Gross total receipts in the protection for that year are not likely to exceed the said amount</p>

Rule 6F(2) prescribes the books to be maintained are as follows :-

- Cash Book
- Ledger
- Journal (if mercantile system is adopted)
- Bills and vouchers in respect of expenses incurred
- Copies of bills issued for amounts exceeding ₹ 25.

In case of medical practitioner, the following additional books are to be maintained.

- Daily case register (Form 3C)
- Inventory as on the first and last day of the Previous Year, showing the stock of medicines (where drugs and medicines are dispensed during the course of practice)

Rule 6F(5) provides that the books of account and documents are required to be kept for eight years from the end of the relevant Assessment Year and for cash book and ledger for a period of 16 years

In case of assessment relating to any Assessment Year reopened u/s. 147 of the I.T. Act within the period specified in section 149 of the Act, the books and documents relating to that year are required to be kept and maintained till the assessment so reopened has been completed.



AUDIT OF ACCOUNTS [Sec. 44AB]

In case of following person carrying on business or profession are required to get his accounts audited before the specified date by an accountant and to furnish such report in the prescribed form duly signed and verified by such accountant and setting forth such particulars as may be prescribed before the specified date.

- Carrying on business where total sales turnover or gross receipts exceeds ₹60,00,000;
- Carrying on profession where gross receipts exceed ₹ 15,00,000; or
- Carrying on business referred to in section 44AD or 44AE or 44AF and claiming his income to be lower than the income prescribed under the relevant section.

Types of Audit report [Rule 6G]

Form No. 3CA : For the person who carries on Business or Profession and who is required by or under any other law to get his accounts audited.

Form No. 3CB : For the person carrying on Business or Profession who are not required to get his account audited under any other law.

Form No. 3CD : The particulars of which are required to be furnished u/s. 44AB.

SPECIFIED DATE [EXPLANATION TO SEC. 44AB]

“Specified date” in relation to the accounts of the assessee of the Previous Year relevant to the Assessment Year, means the 30th September of the Assessment Year.

It may also be noted that the requirement of Audit u/s. 44AB does not apply to person who derives income referred to in Sec. 44B, 44BB, 44BBA and 44BBB.

In case of an agent who earns only commission income, the audit of accounts is required only if the commission exceeds ₹ 60 lakhs. [CBDT circular No. 452 dt. 17.3.1986]

INCOME PARTLY AGRICULTURE AND PARTLY BUSINESS

Rule 7A :	Income from manufacture of Rubber :- 35% of such income shall be deemed to be business income and liable to tax. 65% of such income shall be deemed to be Agricultural income.
Rule 7B :	Income from the manufacture of coffee :- 40% of such income shall be deemed to be business income and liable to tax. 60% of such income shall be deemed to be agricultural income.
Rule 8 :	Income from the manufacture of tea :- 40% of such income shall be deemed to be business income and liable to tax. 60% of such income shall be deemed to be agricultural income.

PRESUMPTIVE INCOME

PROFITS AND GAINS OF BUSINESS OF CIVIL CONSTRUCTION (SEC.44AD)

Applicable only if the gross receipts paid or payable (to the assessee) does not exceed ₹60 lakhs.

Income : 8% of such gross receipts. However, if the assessee, declares higher income, that shall be considered.

PROFITS AND GAINS OF BUSINESS OF PLYING, HIRING OR LEASING GOODS CARRIAGES (SEC.44AE)

Applicable to an assessee who owns not more than 10 goods carriages at any time during the previous year and who is engaged in the business of plying, hiring or leasing of such goods carriages:

- For heavy goods vehicle – ₹ 5,000 for every month or part of a month during which the heavy vehicle is owned by the assessee in the previous year.
- For goods carriage other than heavy goods vehicle – ₹ 4,500 for every month or part of a month during which the goods carriage is owned by the assessee.

Presumptive income for truck owners [Section 44AE] [W.e.f A.Y. 2011-12]

Under the existing provisions of section 44AE, a presumptive scheme is available to assesses engaged in business of plying, hiring or leasing goods carriages. The scheme applies to an assessee, who owns not more than 10 goods carriages at any time during the previous year.

The Act has enhanced the presumed income per vehicle for the owners of—

- (i) Heavy goods vehicle to ₹ 5,000 p.m.; and
- (ii) Other than heavy goods vehicles to ₹ 4,500 p.m.

The Act has further provided an anti-avoidance clause stating that a prescribed fixed sum or a sum higher than the aforesaid sum claimed to have been earned by the assessee shall be deemed to be profits and gains of such business.

Presumptive income scheme for retail business merged with section 44AD [Section 44AF] [W.e.f. A.Y. 2011-12]

SPECIAL PROVISIONS FOR COMPUTING PROFITS & GAINS FOR NON-RESIDENTS

Section	Nature of Business	Profit- % on Turnover
44B	Shipping business in case of non-resident.	7-1/2%
44BBB	Business of providing services or facilities in connection with or supplying plant and machinery on hire used in the prospecting for or extraction or production of mineral oils in case of non-resident.	10%
44BBA	Business of operation of aircraft in case of non-resident.	5%
44BBB	In case of foreign company engaged in i) Civil construction ii) erection of plant or machinery iii) testing or commissioning thereof in connection with turnkey power project approved by the Central Government, income is determined at 10% of the gross amount.	10% of the gross amount paid or payable in India or out of India.

REQUIREMENT AS TO MODE OF ACCEPTANCE, PAYMENT OR REPAYMENT IN CERTAIN CASES TO COUNTERACT EVASION OF TAX

Mode of taking or accepting certain loans and deposits [Sec. 269SS]

No person shall, after the 30th day of June, 1984, take or accept from any other person (hereafter in this section referred to as the depositor), any loan or deposit otherwise than by an account payee cheque or account payee bank draft if,—

- (a) the amount of such loan or deposit or the aggregate amount of such loan and deposit ; or
- (b) on the date of taking or accepting such loan or deposit, any loan or deposit taken or accepted earlier by such person from the depositor is remaining unpaid (whether repayment has fallen due or not), the amount or the aggregate amount remaining unpaid ; or
- (c) the amount or the aggregate amount referred to in clause (a) together with the amount or the aggregate amount referred to in clause (b), is twenty thousand rupees or more :

Provided that the provisions of this section shall not apply to any loan or deposit taken or accepted from, or any loan or deposit taken or accepted by,—

- (a) Government ;
- (b) any banking company, post office savings bank or co-operative bank ;
- (c) any corporation established by a Central, State or Provincial Act ;
- (d) any Government company as defined in section 617 of the Companies Act, 1956 (1 of 1956) ;
- (e) such other institution, association or body or class of institutions, associations or bodies which the Central Government may, for reasons to be recorded in writing, notify in this behalf in the Official Gazette :



Provided further that the provisions of this section shall not apply to any loan or deposit where the person from whom the loan or deposit is taken or accepted and the person by whom the loan or deposit is taken or accepted are both having agricultural income and neither of them has any income chargeable to tax under this Act.

Mode of repayment of certain loans or deposits [Sec. 269T]

No branch of a banking company or a co-operative bank and no other company or co-operative society and no firm or other person shall repay any loan or deposit made with it otherwise than by an account payee cheque or account payee bank draft drawn in the name of the person who has made the loan or deposit if—

- (a) the amount of the loan or deposit together with the interest, if any, payable thereon, or
- (b) the aggregate amount of the loans or deposits held by such person with the branch of the banking company or co-operative bank or, as the case may be, the other company or co-operative society or the firm, or other person either in his own name or jointly with any other person on the date of such repayment together with the interest, if any, payable on such loans or deposits, is twenty thousand rupees or more :

Provided that where the repayment is by a branch of a banking company or co-operative bank, such repayment may also be made by crediting the amount of such loan or deposit to the savings bank account or the current account (if any) with such branch of the person to whom such loan or deposit has to be repaid :

Provided further that nothing contained in this section shall apply to repayment of any loan or deposit taken or accepted from—

- (i) Government;
- (ii) any banking company, post office savings bank or co-operative bank;
- (iii) any corporation established by a Central, State or Provincial Act;
- (iv) any Government company as defined in section 617 of the Companies Act, 1956 (1 of 1956);
- (v) such other institution, association or body or class of institutions, associations or bodies which the Central Government may, for reasons to be recorded in writing, notify in this behalf in the Official Gazette.

Mode of repayment of Special Bearer Bonds, 1991 [Sec. 269TT]

Notwithstanding anything contained in any other law for the time being in force, the amount payable on redemption of Special Bearer Bonds, 1991, shall be paid only by an account payee cheque or account payee bank draft drawn in the name of the person to whom such payment is to be made.

Income from business or Profession and Tax Planning

Following are certain measures should be kept in mind for tax planning for income from business or profession.

1. Nature of business: Economic factors such as scope, profitability, feasibility factors, etc. are important for determining the nature of business but the benefits and concessions available to each line of business may also be presumed before expanding an existing line of business.
2. Location of business: Although certain factors such as nearness to the source of raw materials or markets or availability of infrastructure may be useful in taking decision on the location of business, tax consideration is also equally important. If an industry is located in backward area, deduction under section 80-IB is available.
3. Sources of funds: There are different sources of funds depending upon the needs, availability, terms, etc. However for availing the tax benefits, there should be proper debt- equity mix in the capital structure and a clear policy on return on capital employed.
4. Travel Expenses: The travel expenses of spouse were held as inadmissible, if such travel is not for business consideration. She may be made a partner in the firm to claim business expenditure on travel and further the share of profit of the spouse cannot be clubbed with that of the husband as the same is exempt u/s 10(2A).
5. Employee welfare funds: The contribution of the employees' welfare funds should be paid within time limits prescribed under the relevant Acts. It would be better to borrow and pay the tax liability on or before relevant due date. Contribution made to the welfare funds after the due date does not qualify for deduction even in the year of payment. However interest on money borrowed for meeting such liability qualifies as business expenses.

SHORT QUESTIONS & ANSWERS ON PROFITS AND GAINS FROM BUSINESS OR PROFESSION

State the deductibility of the following expenses :

- 1) Anticipated hedging loss under a contract to purchase raw material.
- 2) Non-recovery of a bill due to negligence of an employee.
- 3) Initial expenditure incurred on installation of fluorescent tube lights.
- 4) Non-recovery of advance allowed to 100% subsidiary company engaged in the business of financing subsidiary companies.
- 5) Consultation fees paid to tax advisor.
- 6) Lump sum payment made to acquire a licence regarding technical information to reduce the production cost.
- 7) Payment made to catering agency for providing food/beverages to employees, working in overtime @ ₹ 75 per employee for 20 days.
- 8) Subsidy received from the government to compensate the loss suffered in exports under government sponsored scheme, has been directly credited to Capital Reserve A/c. The assessee claims it as exempt.
- 9) Compensation paid to an employee under voluntary retirement scheme which does not conform to the guide lines under Sec. 10(10C).
- 10) Commission accrued during the year but not credited in books as it has been held back due to breach of certain conditions, which may create liability to pay damages.
- 11) Rent of quarters, located near factory, let out to the employees of the factory, was treated as income from house property.
- 12) Fees of ₹ 30,000 were paid by the company to a lawyer to defend the company in a court case. Lawyer is the brother of the director of the company. The fees have been paid by a bearer cheque and it is found excessive to the extent of ₹ 20,000.
- 13) Employees contribution to the recognised provident fund, ₹ 60,000 has been charged to the profit and loss account but only ₹ 25,000 was credited to their accounts on due date and the balance was credited to their account on the due date fixed for furnishing return of income for the relevant previous year.
- 14) Bonus/commission to employees was paid: (a) during the previous year; or (b) after the previous year but on or before the due date of return of income for that year, or (c) after the due date the return of income for that previous year.
- 15) Salary has been paid to a resident employee outside India and non-resident employee in India but no tax has been paid thereon or deducted therefrom.
- 16) Advertisement expenses incurred outside India in foreign currency. RBI permission has not been obtained.
- 17) Municipal taxes and land revenue in respect of staff quarters were paid after due date of furnishing return of income for the relevant previous year.
- 18) Foreign tour expenses of the managing director for 10 days. However, 2 days were devoted to personal work.
- 19) Advertisement in a journal published by political party.
- 20) 600 VIP brief cases, costing ₹1,500 each, presented to customers.
- 21) Voluntary payment of gratuity paid an account of commercial expediency to an employee who died on business tour.
- 22) Traveling expenses to explore the feasibility of new line of business.
- 23) Annual payments in installments over a period of 10 years to seek assistance in technical know-how for improving quality of product.
- 24) Expenses incurred for registration of trademarks.
- 25) Employees were issued shares at par to protect business interest. Difference of market price and par value was charged as revenue expenditure.
- 26) Expenditure incurred on neon-sign board for the business premises.



- 27) Theft of stock-in-trade assuming (a) it is insured (b) it was uninsured
- 28) Expenditure incurred for new telephone connection.
- 29) Purchase of sanitary and pipeline for factory
- 30) Legal charges incurred for framing the scheme of amalgamation of C company with the assessee company.
- 31) Compensation paid to cancel the purchase order of a machine due to abnormal rise in its price. The assessee claims it as trading loss, or capital loss.
- 32) Confiscation of goods, imported without a valid import licence. The assessee was also fined by custom authorities. The assessee claims deduction for both of them under general deductions Sec. 37(1).
- 33) The assessee claims the set-off unabsorbed depreciation of a discontinued business against the profits of another business.

Solution :

- 1) Anticipated hedging loss under a forward contract is not allowed to be deducted.
- 2) Loss caused due to negligence of employee is allowed to be deducted.
- 3) Initial expenditure on installation of fluorescent tube lights is a capital expenditure, not deductible [Sec. 37(1)].
- 4) As the business of 100% subsidiary is to finance subsidiary company, loss on account of non-recovery of such advances relates carrying on business. Such loss is an allowable deduction.
- 5) Consultation fee paid to tax-advisor is allowed under Sec. 37(1).
- 6) Payment made to acquire licence regarding technical information is a capital expenditure. Depreciation is allowed under Sec. 32 on such cost.
- 7) Payment made to catering agency to provide food/beverages to employees is allowed under Sec. 37(1). However, the employer becomes liable to pay Fringe Benefit Tax.
- 8) Subsidy granted by government against loss suffered by exporters under government-sponsored scheme, is a trading receipt. Recovery of loss is taxable under Sec. 41(1).
- 9) Compensation paid under voluntary retirement scheme is allowed to be deducted in five equal annual instalments [Sec. 35DDA]. Scheme of voluntary retirement need not be in accordance with the guidelines of Sec. 10(10C).
- 10) Commission accrued during the year is taxable under mercantile system. Liability to pay damages for breach of certain conditions is a contingent liability. No deduction can be allowed for such provision.
- 11) Rent from quarters, let out to employees, is a business income provided the letting is subservient and incidental to the main business.
- 12) Payment made by a company to the brother of the director of the company, is covered under Sec. 40A(2). Therefore, excessive fees of ₹ 20,000 have to be disallowed. Provisions of Sec. 40A(3) apply to the balance payment since it has been made by bearer cheque. Accordingly, the balance of ₹20,000 shall have to be disallowed in computing taxable business profits, w.e.f. A.Y.2010-11.
- 13) Deduction is allowed for employees' contribution credited to their account on the due date under provident fund rules. No deduction is allowed for such contribution credited to their account thereafter. Employees' contribution, deducted from their salaries, is first treated as business income. If the same has not been credited to their account, the same has to be treated business income first.
- 14) Bonus/commission paid to the employees during the previous year or paid after the previous year but before the due date fixed for furnishing return of income for the previous year is allowed to be deducted in the same previous year in which the liability to pay such bonus/commission arose. Any bonus/commission, paid to employees after such due date, is allowed to be deducted in the previous year in which the date of payment falls.

- 15) Salary paid to any person outside India (resident or non-resident) or salary paid to a non-resident in India is not allowed to be deducted if tax has not been paid thereon nor deducted therefrom [Sec. 40(a)(iii)]. Thus, no deduction is allowed in the instant case. It is operative from the assessment year 2006-2007.
- 16) Advertisement expenditure incurred in India or outside India is allowed to be deduction under Sec. 37(1) provided it is not of capital nature and it is incurred wholly and exclusively for the purposes of business. Permission of RBI is not relevant.
- 17) Deduction of municipal taxes and land revenue in respect of staff quarters, will be deducted in the previous year in which the date of payment falls (Sec. 43B).
- 18) Proportionate foreign tour expenses of the director relating to personal work are not to be allowed; such expenditure has not been incurred wholly and exclusively for the purposes of business. However, air fare (both ways) will be fully allowed.
- 19) No deduction can be allowed for advertisement in the journals published by a political party [Sec. 37(2B)].
- 20) Presentation of VIP bags to customers is allowed as expenditure on advertisement under Sec. 37(1). There is no ceiling limit for gift articles.
- 21) Voluntary payment of gratuity on account of commercial expediency is allowable deduction under Sec. 37(1).
- 22) Travelling expenditure for exploring new line of business is a capital expenditure. It is not allowed under Sec. 37(1). It may be capitalised for the purposes of Sec. 35D.
- 23) Annual instalment paid for technical know-how is a revenue expenditure. It is allowed under Sec. 37(1).
- 24) Expenses incurred for registration of trademark is a revenue expenditure. It is, therefore, allowed under Sec. 37(1).
- 25) Waiver of premium while issuing shares to employees, is not a trading transaction. It is not deductible.
- 26) Expenditure incurred on neon-sign board is a capital expenditure. It is not allowed in computing business income [(Sec. 37(1))]. However, depreciation can be claimed on it @ 15%.
- 27) Loss of stock-in-trade due to theft is allowed under Sec. 29 as incidental to business. However, if it is insured insurance compensation will be a trading receipt.
- 28) Expenditure on new telephone lines is allowed under Sec. 37(1). It is a revenue expenditure incurred for the purposes of business.
- 29) Purchase of sanitary pipe-line is a capital expenditure, not allowable under Sec. 37(1). However, depreciation is allowed under Sec. 32 @ 15%.
- 30) Amalgamation expenses are allowed to be deducted in computing taxable profits under Sec. 35DD in five equal annual instalments.
- 31) Compensation paid to cancel the purchase order of a machine, is a capital expenditure. It avoids futile investment in machine. It cannot be deducted under Sec. 37(1). As there is no "transfer" of a capital asset, compensation paid cannot be claimed as a capital loss also.
- 32) Explanation to Sec. 37(1) does not allow any illegal expense in computing taxable profit of business. Therefore, fine imposed for illegal import cannot be allowed [Explanation to Sec. 37(1)]. However, loss by way of the confiscation of goods can be allowed as incidental to business under Sec. 29.
- 33) Unabsorbed depreciation of a discontinued business now can be set-off against the profits of any other business and thereafter against the income of any other head. It is operative from the assessment year 2003-2004.


PROBLEMS ON PROFITS AND GAINS FROM BUSINESS OR PROFESSION

Illustration 20 : Mr Sameer, resident in India, for the year ending on 31 March 2012. Compute his income from business and gross total income for the assessment year 2012-2013.

Profit & Loss Account for the year ended 31.3.12
Dr.
Cr.

Expenditure	₹	Receipts	₹
To purchases	1,90,000	By sales less returns	5,69,300
To salaries and wages	1,40,000	By bad debts recovered,	2,000
To trade expenses	1,000	allowed in earlier years by the	
To purchase of trademarks	50,000	Assessing Officer	
To registration of trademarks	2,000	By interest on securities (gross)	892
To rent, rates and taxes	5,000	By dharmada, mandir and	2,000
To discount allowed	1,500	gaushala receipts	
To household expenses	6,000	By refund on income tax	1,008
To advertisement bill paid in cash	30,000	By proceeds of life insurance	43,500
To income tax	10,000	policy on maturity	
To sales tax paid	3,000		
To purchased technical know-how	12,000		
To expenses incurred on income	15,100		
tax and sales tax proceedings			
To contribution paid to a trust for	1,000		
staff welfare			
To staff welfare expenses incurred	700		
To OYT deposit	5,000		
To postage and telegrams	1,300		
To donation to National Defence Fund	2,500		
To life insurance premium on the	2,000		
life of the assessee			
To interest on capital	5,000		
To interest on loan taken to pay	500		
income tax			
To wealth tax	500		
To audit fee	1,000		
To entertainment expenditure	30,000		
To gifts and present to five customers,	15,000		
costing ₹ 3,000 each			
To expenses on apprentice training	4,000		
To emergency risk insurance	200		
To fire insurance premium for stock	200		
To provision for bad and doubtful debts	3,000		
To reserve for pecuniary losses	5,000		
To net profit	76,000		
Total	6,18,700		6,18,700

Solution :

Assessee : Mr. Sameer

Computation of Gross Total Income

A. Y : 2012-2013

Particulars	₹	₹
Income from Business		
Net profit as per profit and loss account		76,000
Add: Expenses inadmissible in computing profits and gains from business or profession:		
Purchase of trademarks	50,000	
Household expenses [Sec. 37(1)]	2,500	
Advertisement bills paid in cash [Sec. 37(1) r.w. Sec. 40A(3)] @ 100% of ₹ 30,000	30,000	
Income tax [Sec. 40(a)(ii)]	10,000	
Purchase of technical know-how	12,000	
Contribution to a Trust for staff welfare fund [Sec. 40A(9)]	1,000	
Donation for National Fund [Sec. 37(1)]	2,500	
Life Insurance premium [Sec. 37(1)]	2,000	
Interest on capital [Sec. 36(1)(iii)]	5,000	
Interest on loan to pay income tax [Sec. 37(1) r.w. 40(a)(ii)]	500	
Wealth tax [Sec. 40(a)(iii)]	500	
Provision for bad and doubtful debts [Sec. 37(1) r.w. 36(1)(vii)(2)]	2,000	
Reserve for pecuniary losses [Sec. 37(1)]	6,000	
	<u>1,24,000</u>	<u>1,24,000</u>
		2,00,000
Less:		
(a) Income not relating to business or profession: [Sec. 28(i)]	892	
Interest on government securities		
(b) Dharada, mandir and gaushala receipts	2,000	
(c) Refund of income tax	1,008	
(d) Proceeds of L.I.P.: It is not a business receipt and exempt [Sec. 10(10)]	43,500	
(e) Depreciation on trademarks; 25% of ₹ 50,000	12,500	
(f) Depreciation on know-how: 25% of ₹ 12,000	<u>3,000</u>	<u>59,400</u>
Income from business		<u>1,40,600</u>
Statement of Gross Total Income for the Assessment Year 2012-2013		
1. Income from business		1,40,600
2. Income from other sources— Interest on securities		892
Gross Total Income		<u>1,41,492</u>

Note :

- 1) Bad debts deducted in earlier years and now recovered, has been rightly included in the profit and loss account as business income [Sec. 41(4)].
- 2) Since payment of income tax is not deductible, its refund cannot be taxed as deemed profits [Sec. 41(1)].
- 3) OYT (own your telephone) deposit is an allowable deduction in the year in which it is paid.



- 4) "Dharmada", "mandir" and "gaushala" receipts are customarily levies by trader for charitable purposes. Amount received under these heads are not trading receipts. The fact that the amount collected under these heads are spent for other purposes would amount to breach of trust but it would not affect the initial nature and character of the receipt. Such receipts are not taxable.
- 5) The assessee is entitled to the deduction in respect of donation to National Defence Fund under Sec. 80G.
- 6) Life insurance paid by assessee on his life is allowed to be deducted in imputing total income under Sec. 80C.
- 7) Any payment on advertisement exceeding ₹ 20,000 should be made by on account payee cheque or account payee bank draft. Since the payment has been made in cash, 100% of advertisement has been disallowed [Sec. 37(1) r.w. Sec. 40A(3)]. 'Crossed cheque' requirement has been amended by 'account payee' cheque. It is operative from 13-07-2008.
- 8) From the assessment year 2001-2002, intangible assets also fall within the scheme of depreciation. Hence, depreciation has been allowed on trademarks and know-how.
- 9) Registration expense of trademarks is revenue expenditure, allowed under Sec. 37(1).

Illustration 21 : Dr L.Kochagaway is a renowned medical practitioner. He furnishes his receipts and payments account for the previous year 2011-2012 :

Dr.

Cr.

Receipts	₹	Payments	₹
To balance b/d	35,000	By rent of clinics:	
To consultation fees :		2009-2010	13,600
2009-2010	25,000	2010-2011	44,800
2010-2011	1,80,000	2011-2012	<u>26,600</u>
2011-2012	<u>2,62,000</u>		85,000
	4,67,000	By electricity and water	12,000
To visiting fees	1,30,000	By purchase of professional books	18,000
To loan from bank for	2,25,000	By household expenses	97,800
professional purposes		By municipal taxes paid in respect	12,000
To sale of medicines	1,73,000	of property	
To gift/presents from patients	15,000	By purchase of motor car	2,45,000
To remuneration from articles	26,000	By Telephone Charges	10,000
published in professional		By fire insurance in respect of	3,200
magazines		property	
To rent from house property	96,000	By surgical equipment	44,700
To interest on Post Office National	17,000	By advance income tax	43,000
Savings Certificates		By salary and perquisite to	72,000
		compounder	
		By entertainment expenses	16,000
		By purchase of X-ray machine	2,00,000
		By expenses of income-tax	15,000
		proceedings	
		By life insurance premium	25,000
		By gifts to wife	25,000
		By interest on loan	12,000
		By loan a/c—instalment paid	25,000
		By donation to Political Party	2,500
		By car expenses	36,000
		By purchase of medicines	1,05,000
		By balance c/d	79,800
	<u>11,84,000</u>		<u>11,84,000</u>

Compute his income from profession and gross total income for the assessment year 2012-2013 after taking into account the following additional information:

1. One-third of the car expenses are in connection with personal use.
2. Depreciation on motor car is allowed at the rate of 15%.
3. The construction of the house property was completed in March 2007. It was let out for residential purposes.
4. Expenses on income tax proceeding include ₹ 1,000 paid for the preparation of return of income.
5. Receipts outstanding from patients for 2011-2012, amount to ₹ 8,000.
6. Closing stock of medicines is ₹ 8,000 but its current market price is ₹ 12,000.
7. Books purchased include annual publications of ₹ 12,000, purchased in December 2011.

Solution : (a) Computation of income from profession for the assessment year 2012-2013 :

Particulars	₹	₹
Income from Profession :		
(a) Receipt from profession:		
1. Consultation fees: [Sec. 28(i)]: (₹ 25,000 + ₹ 1,80,000 + ₹ 2,62,000)	4,67,000	
2. Visiting fees [Sec. 28(i)]	1,30,000	
3. Sale of medicines [Sec. 28(i)]	1,73,000	
4. Gifts and presents from patients [Sec. 28(iv)]	15,000	
5. Remuneration from articles published in professional magazines [Sec. 28(i)]	26,000	
		8,11,000
(b) Closing stock of medicines		8,000
Total receipts and closing stock		8,19,000
Less: Expenses allowable:		
1) Rent of clinic [Sec. 30]	85,000	
2) Electricity and water [Sec. 37(1)]	12,000	
3) Salary of compounder [Sec. 37(1)]	72,000	
4) Entertainment expenses [Sec. 37(1)]	16,000	
5) Expenses on income-tax proceedings [Sec. 37(1)]	15,000	
6) Interest on loan [Sec. 37(1)(iii)]	12,000	
7) Purchase of medicines [Sec. 37(1)]	1,05,000	
8) Car expenses [Sec. 37(1)] (2/3 × ₹ 36,000)	12,000	
9) Depreciation on professional books :		
(i) Annual publications: 12,000 × 100% × 50%	6,000	
(ii) Other books: 6,000 × 60%	3,600	
10) Depreciation on car [Sec. 32 r.w. Sec. 38] : 15% of 2,45,000 × 2/3	24,500	
11) Depreciation on plant and machinery:		
(i) X-ray machine	2,00,000	
(ii) Surgical equipment	44,700	
Depreciation @ 15% of	2,44,700	
12) Telephone Charges	10,000	
Taxable Income from Profession		4,09,195



	B/F	4,09,195
Computation of Income from House Property :		
Gross annual value on the basis of rental valuation	96,000	
Less: Full municipal taxes paid by the owner	12,000	
Net annual value	84,000	
Less: Statutory deduction: 30% of net annual value	25,200	
	58,800	
Income from House Property		58,800
Gross Total Income		4,67,995
Less: Deduction u/s 80C (LIC premium paid)		25,000
Less: Deduction u/s 80GGC		2,500
Actual amount of donation to political party		
Total Income		4,40,495
Total Income rounded off u/s 288A		4,40,490

Notes :

- Purchase of motor car is capital expenditure. Hence, it is not deductible. Depreciation has been allowed on motor car.
- Plant includes books and surgical equipment. Depreciation on professional books is allowed @ 60% but annual publications are written off @ 100%. However, as annual publications have been put to use for less than 180 days during the year, depreciation has been allowed @ 50%. The assessee can claim depreciation on surgical equipment at general rate.
- Contribution of articles to periodicals and magazines constitutes income from vocation of the assessee.
- Expenses in income-tax proceedings are wholly deductible [Sec. 37(1)].
- One-third of car expenses and proportionate depreciation in respect of motor car have been disallowed as they are in connection with the personal use of the assessee.
- Interest on Post Office National Saving Certificates is exempt from income tax [Sec. 10(15)].
- Profits and gains of the business or profession are computed according to the method of the accounting regularly followed by the assessee (Sec. 145). Since the assessee has adopted cash system of accounting, "Income" is taxable on receipt basis and "expenditure" is allowed to be deducted on payment basis, irrespective of the previous year to which the receipt of payment belongs. Receipts outstanding for the previous year 2010-2011 will not be taken into consideration.
- Profits and gains of business profession is required to be computed according to the system of accounting regularly followed by the assessee but if the income cannot be properly deduced therefrom, the Assessing Officer may compute the income on such basis and in such manner as he may deem fit [Proviso to Sec. 145(1)].

In view of this, the Assessing Officer may take into account the value of closing stock while determining profits even under cash system of accounting

- Donation to Political Party is allowed to be deducted from gross total income under Sec. 80GGC.

Illustration 22 : The Profit and Loss Account of RAI & Co. for the previous year 2011-2012 is given as follows :

Particulars	₹	Particulars	₹
Purchases of goods	10,00,000	Sale of goods	26,00,000
Salaries, bonus and commission	8,00,000	Closing stock	50,000
Rent, rates and taxes	60,000	Interest on drawings	7,000
Depreciation @ 16% on WDV	20,000	Interest on securities	20,000
Travelling expenses	1,50,000		
Interest on capital	25,000		
Advertisement	1,20,000		
Entertainment expenses	60,000		
Expenditure on neon-sign board	50,000		
New telephone deposit under OYT scheme	5,000		
Compensation for cancelling purchase order of an outdated machine	10,000		
Expenses for promoting family planning among employees	20,000		
Net profit	3,57,000		
	<u>26,77,000</u>		<u>26,77,000</u>

Additional Information :

- (i) Salaries, bonus and commission include: ₹
- (a) Salary to the proprietor 1,50,000
- (b) Bonus paid to employees on 15-10-2012 75,000
- (c) Salary of ₹ 1,20,000 was paid in India to B, a non-resident employee but neither any tax was deducted at source nor paid thereon. However, B is a PAN holder and has cleared his tax liability.
- (d) Advertisement includes:
- (i) a hoarding bill paid in cash, ₹ 38,000
- (ii) advertisement published in souvenir, published by a political party ₹10,000
- (e) Depreciation has been charged on plants and machinery and furniture and fittings in proportion of 3:2. Depreciation @ 15% on plant and @10% on furniture.
- (f) Purchases include goods of ₹1,00,000, imported without a licence and confiscated by the customs authorities.
- (g) Travelling expenses include a sum of ₹1,00,000 on foreign travel to purchase a machine. Negotiations have not been finalized.
- (h) Annual stock taking revealed a theft of goods, costing ₹30,000.
- (i) This year stock valuation was deviated from the market price to cost price which is 20% less than its market price.

Compute taxable business profits for the Assessment year 2012-13.



Solution :

Computation of Taxable Business Profits for the Assessment Year 2012-2013

Particulars	₹	₹
Income from Business		
Net profit as per profit and loss account		3,57,000
Add: <u>Inadmissible Expenses</u>		
(a) Salary paid to Proprietor	1,50,000	
(b) Bonus paid to employees: Deduction will be allowed in Previous Year 2012-13 (Sec.43B, being disallowance of unpaid liability)	75,000	
(c) Salary paid to non-resident employee, without deducting or paying TDS[Sec.40(a)(iii)]	1,20,000	
(d) Advertisement bills paid in cash [Sec. 37(1) r.w. Sec. 40A(3)] @100% of ₹ 38,000	38,000	
(e) Advertisement in souvenir published by political party [Sec.37(2B)]	10,000	
(f) Depreciation to be treated separately	20,000	
(g) Expenses on family planning: allowable only to a company assessee [Sec.36(1)(ix)]	20,000	
(h) Foreign travel to acquire a new machine, (being capital in nature, deal not yet finalized. It may be added to the cost of the asset when such asset is actually procured)	1,00,000	
(i) Interest on capital [Sec. 36(1)(iii)] [There is no borrowings]	25,000	
(j) Expenditure on neon sign board, being a capital expenditure on advertisement, hence disallowed.	50,000	
(k) Compensation paid to cancel a capital liability, capital in nature, hence disallowed u/s 37(1)	10,000	
(l) Under valuation of closing stock:[50,000/80% - 50,000]	12,500	
	<u>12,500</u>	<u>6,30,550</u>
Less: Expenses allowed :		<u>9,87,500</u>
Interest on Drawings		7,000
Depreciation u/s 32:		
(a) Plant and machinery:		
WDV on 01.04.2011 : $20,000 \times 4/5 \times 100/16$	1,00,000	
Add: Cost of neon-sign board	<u>50,000</u>	
	1,50,000	
Less: Depreciation @15%	<u>22,500</u>	22,500
WDV as on 31.3.12	<u>1,27,500</u>	
(b) Furniture and Fittings:		
WDV on 01/04/11 : $20,000 \times 1/5 \times 100/16$	25,000	
Less: Depreciation @10%	<u>2,500</u>	2,500
WDV on 31.3.2012	<u>22,500</u>	
Less: <u>Incomes credited to Profit and Loss A/c to be treated under separate Head of Income</u>		
Interest on Government Securities		<u>20,000</u>
Taxable Business Profits		<u>9,35,500</u>

Note :

- (1) Loss due to theft of stock-in-trade is allowable in computing business profits u/s 29. Such loss is incidental to business operation. Since purchase of goods have already been debited to profit and loss account, no separate adjustment is required.
- (2) Loss in illegal business may be allowed u/s 29. Explanation to Sec.37(1) does not apply to Sec. 29.
- (3) Deposit for new telephone connection is allowable u/s 37(1). Hence, no adjustment is required.

Illustration 23 : The Profit & Loss Account of Mr.Dipak Sinha for the previous year 2011-2012 is given below :

Dr.

Cr.

Particulars	₹	Particulars	₹
Cost of goods sold	16,00,000	Sales	34,70,000
Salaries wages	9,00,000	Rent of staff quarters	3,00,000
Rent of business premises, owned by the assessee	2,50,000	Sale price of machinery block on 31-03-2011	5,00,000
Repairs and renewals	1,40,000		
Income tax paid	60,000		
Excise duty paid	1,00,000		
Sales tax payable	2,00,000		
Legal expenses	3,00,000		
Municipal taxes payable for staff quarters	10,000		
Provision for bad debts	60,000		
Contingency reserve	1,00,000		
Employees contribution to recognised fund	50,000		
Net profit	5,00,000		
	<u>42,70,000</u>		<u>42,70,000</u>

Additional Information :

- (i) Salaries include:
 - (a) ₹ 1,20,000 was paid outside India to an employee, "resident" in India but neither tax was deducted nor tax has been paid thereon,
 - (b) ₹ 90,000 was paid in India to an employee "resident" in India but neither tax deducted therefrom nor paid thereon.
- (ii) Excise duty of ₹ 50,000 for the assessment year 2011-2012 was paid on 1 January 2012 but it was not included in the profit and loss a/c.
- (iii) Sales tax amounting ₹ 1,30,000 was paid on 31 July 2012 and the balance was paid on 1 August 2012, the due date of furnishing return of income is 31 July 2012.
- (iv) Repairs/renewals include remodelling and renovation costing ₹ 80,000.
- (v) Legal expenses include:
 - (a) Lawyer fee of ₹ 50,000 paid by bearer cheque to K, nephew of the proprietor. The Assessing Officer disallowed a sum of ₹ 10,000, being found in excess of the desired qualifications;
 - (b) Gift of ₹ 1,20,000, made to wife, a tax-advisor, but disallowed by the A.O.
- (vi) Employees contribution include:
 - (a) ₹ 30,000 credited to their account on due date under Provident Fund rules,
 - (b) ₹ 20,000 credited to their account in November 2012.

- Compute taxable profits for the previous year 2011-2012.

Computation of Business Profits for the Assessment Year 2012-13

Note :

No capital loss, whether short-term or long term, can be set-off against any income. It is to be carried forward for next 8 assessment years.

Illustration 24 : The firm of M/s Amal & Associates is engaged in the business of growing and manufacturing tea. The Profit & Loss Account for the year 2011-2012 is given as follows:

Dr.

Cr.

Particulars	₹	Particulars	₹
Cost of growing and manufacturing tea	40,00,000	Sales	95,00,000
Salaries and wages	15,00,000	Stock	13,50,000
Advertising	5,00,000		
Entertainment expenses	1,00,000		
Travelling expenses	3,00,000		
Fine and penalties	50,000		
Cost of patent rights	6,00,000		
Expenses on scientific research	6,00,000		
General and sundry expenses	2,00,000		
Net profit	30,00,000		
	<u>1,08,50,000</u>		<u>1,08,50,000</u>

You are further informed :

- (i) Advertising includes payment of ₹ 2,00,000 made to a political party for insertion of advertisement in party's journal. The payment has been made by bearer cheque,
- (ii) Travelling expenses include a visit of the director to UK for 10 days (including 2 days for travelling). Five days were utilized for business purpose. Permission for foreign exchange was granted for ₹ 50,000. Total expenditure on the visit is ₹ 1,00,000 (including air fare of ₹ 40,000).
- (iii) Expenses on scientific research include:
 - (a) Purchase of land ₹ 1,50,000
 - (b) Contribution to Agricultural Research Institute, New Delhi which is a National Laboratory ₹ 20,000.
 - (c) Contribution to Bhaba Atomic Research Centre (an approved research association) for statistical research, which is not related to business ₹ 30,000.
- (iv) Refund of custom duty, deducted in the previous year, 2009-2010, amounting to ₹ 50,000, has not been credited to the profit and loss account.
- (v) Sundry expenses include a contribution of ₹ 60,000 to Kolkata Municipal Corporation for undertaking a Drinking Water Project for slum-dwellers. The Project has been approved by National Committee but KMC has not issued any certificate indicating the progress of the project.
- (vi) A deposit of ₹ 12,00,000 was made in instalments with National Bank for Agriculture and Rural Development (a) ₹ 4,00,000 in September 2011, (b) ₹ 6,00,000 in July 2012 and (c) ₹ 2,00,000 in December 2012. It has not been included in the profit and loss account. Date of submitting return of income 30/09/2012.
- (vii) (a) W.D.V. of machinery on 01-04-2011 (Rate of depreciation 15%) ₹15,00,000
 (b) Machinery purchased in December 2011 for scientific research ₹ 5,00,000
 (c) Purchase of five small drier machine, each costing ₹10,000
 (d) Sale price of an old machinery (Rate of depreciation 15%) ₹ 6,00,000
- (viii) Lump sum payment of ₹ 5,00,000 was made to acquire a licence regarding technical information to improve tea-flavour. It has not been charged to P/L a/c.

Compute the taxable business profits for the assessment year 2012-2013.

Solution :

Computation of Business Profits for the Assessment Year 2012-2013

Particulars	₹	₹
Net profit		30,00,000
Add: Inadmissible Expenses:		
1. Advertisement payment to a political party [Sec. 37(2B)]	2,00,000	
2. Travelling outside India [Sec. 37(1)]. Proportionate expenses of foreign travel, (excluding air fare) not relating to business: $60,000 \times 3/8$	22,500	
3. Fine and penalties	50,000	
4. Cost of patent rights	6,00,000	
5. Expenditure on scientific research (Sec. 35): Purchase of land	1,50,000	
6. Contribution to Bombay Municipal Committee (Sec. 35 AC):	60,000	10,82,500
Since the Certificate indicating progress in the prescribed form has not been issued, no deduction is allowed.		40,82,500
Add: Deemed profit: Refund of Customs Duty, deducted in earlier years, not credited in the profit and loss a/c [Sec.41(1)]		50,000
Less: Admissible expenses:		
Capital expenditure on scientific research [Sec.35(1)(iv)(2)]	4,00,000	
Depreciation on Patent rights @ 25% of ₹ 6,00,000	1,50,000	
Depreciation on know-how: @ 25% of ₹ 5,00,000	1,25,000	
Depreciation on Machinery:		
WDV as on 01/04/2011:	15,00,000	
Add: Purchase of driers	50,000	
	15,50,000	
Less: Sale of Old Machinery	5,00,000	
WDV as on 31/3/2012	10,50,000	
Depreciation @ 15% on ₹ 10,50,000		
Weighted Deduction for scientific research:	1,57,500	
(i) National Laboratory: @ 200% of ₹ 20,000 =		
₹ 40,000 – ₹ 20,000 = ₹ 20,000		
(ii) Bhaba Atomic Research Laboratory: @ 175% of ₹ 30,000 =		
₹ 52,500 – ₹ 30,000 = ₹ 22,500		
Therefore, total deduction ₹(20,000 + 22,500)	42,500	8,75,000
Composite Profits before making deduction u/s 33AB		32,47,500
Less: Deposit with NABARD (Sec.33AB)		
Least of the followings:		
(i) Deposit of ₹ 10,00,000 (within the due date of submission of return)		10,00,000
(ii) 40% of Business Profits: 40% of ₹ 32,47,500 = ₹ 12,99,000		
Composite Profits after deduction u/s 33AB		22,47,500
Apportionment of profits into agricultural income and business income (As per Rule 8)[since the assessee is engaged in the business of growing and manufacturing tea:		8,99,000
40% of ₹ 22,47,500		

Illustration 25 : State whether the provisions of Sec. 41(1) of the Act can be applied to a case, where refund of excise duty has been obtained by the assessee on the basis of a decision of the CEGAT and where the matter has been taken up in further appeal to the Court by the Central Excise Department.

Solution : This question has been answered by the Apex Court in *Polyflex (India) Pvt. Ltd. v. CIT* [2003] 257 ITR 343. (SC)

The refund of excise duty pursuant to the decision of the CEGAT would be subject to tax by virtue of Sec. 41(1) and it is not necessary that the revenue should await the verdict of a higher court.

Illustration 26 : In the course of an assessment proceeding, the Assessing Officer enhanced the value of the closing stock and added the difference to the total income.

In the assessment year subsequent to this, the assessee wants the Assessing Officer to enhance, by the same amount, the value of the opening stock of the year.

Discuss the validity of the claim.

Solution : The value of the closing stock of the preceding year must be the value of the opening stock of the succeeding year. Hence, if the value of closing stock at the end of a year is enhanced, the enhanced value should be taken as the value of the opening stock of the next year for the purpose of income tax.

The claim of the assessee in this case is, therefore, valid.

Illustration 27 : What would be your advice regarding admissibility of the following items of expenditure in computing the business income:

- (a) A donation of ₹ 1 lakh made to a University for starting a laboratory for scientific research (i) relating to the assessee's business, (ii) not relating to the assessee's business.
- (b) Travelling expenses include a sum of ₹ 15,000 incurred by a director in travelling abroad for negotiating purchase of plant and purchase of plant and machinery.
- (c) Amount payable as damages to Government on account of shortfall in export target.
- (d) Overdraft from bank for payment of income tax: interest charged by the bank is ₹ 20,000.
- (e) Payment of interest of ₹ 40,000 on monies borrowed from bank for payment of dividends to shareholders.
- (f) ₹ 12,000 paid for shifting of business from the original site to the present place which is more advantageously located.
- (g) Retrenchment compensation of ₹ 4 lakh paid to the workmen on the closure of one of the units.
- (h) Fees paid to the Registrar of Companies for bringing about a change in the Memorandum and Articles of Association in regard to issue of Equity.

Answers :

- (a) The donation has been made to University to be used for scientific research for starting a laboratory. If the University is approved for the purpose of Sec. 35(1)(ii), then irrespective of the consideration whether the scientific research is related to assessee's business or not, deduction could be claimed @ 175% of amount paid. If it is not approved, donation could not be claimed as a deduction under Sec. 35 in the computation of business income. However, the assessee could claim deduction from Gross Total Income under Sec. 80G, if the same is eligible.
- (b) Travelling expenses incurred by the director for negotiating the purchase of plant and machinery is a capital expenditure and hence to be disallowed.
- (c) The payment is not for any infraction of law but for failure to reach a target undertaken by the company being payment made wholly in the course of business, it is deductible.
- (d) Interest on overdraft taken to pay income tax is not allowable under Sec. 36(1)(iii). Interest on borrowings
- (e) utilised for payment of dividend is allowable under Sec. 36(1)(iii).
- (f) Shifting expenses of business premises resulting in an expenditure of enduring benefit is a capital expenditure and is not allowable.



- (g) Retrenchment compensation payable to workmen on the total closure of a business cannot be allowed as deduction as the expenses are not incurred for the purpose of carrying on of its business. When, however, the tax-payer closes one of its units and continues to carry on the same business as before, the compensation will be admissible under Sec. 37(1).
- (h) Fee paid to Registrar of Companies for bringing about change in memorandum and articles of association is a capital expenditure, where it relates to issue of equity shares. Where alterations are warranted by the changes made in the Companies Act, the expenses are allowable.

Illustration 28 : A company engaged in the manufacturing of fertilizer products, commenced its business on 01.04.2011. During the financial years 2008-2009 to 2010-2011 it had incurred ₹ 4.00 lakh annually as expenditure on salaries and purchase of raw material for the purpose of research connected with its business. During the previous year 2011-2012 incurred on scientific research, revenue expenditure of ₹ 3.00 lakh and a capital expenditure of ₹ 4.50 lakh on purchase of plant and machinery. Since the result of the research was unsuccessful, the company sold it its plant and machinery on 31.12.2011 for ₹ 8.00 lakh and closed its research activity. Compute the admissible deduction under Sec. 35 for the assessment year 2012-2013.

Solution :

Computation of deduction u/s 35 for Expenditure on scientific research

Particulars	₹	₹
Expenditure incurred during the earlier 3 years on salaries and purchase of raw material for the purpose of research connected with the business— fully allowed in the year of commencement of business by virtue of Explanation to Sec. 35(1)(i) : [₹ 4,00,000 × 3]		12,00,000
Revenue expenditure on scientific research incurred during the previous year 2011-2012	3,00,000	
Capital expenditure on scientific research incurred during the previous year 2011-2012	4,50,000	
	<u>7,50,000</u>	
Total Weighted deduction @ 200% on ₹ 7.50 lakh u/s 35(2AB)		15,00,000
Admissible deduction u/s 35 for the A.Y. 2012-2013		<u>27,00,000</u>

Illustration 29 : A company engaged in pharmaceuticals manufacturing, debited to its profit and loss account a sum of ₹ 50,000, being the interest on loan of ₹ 5,00,000 taken for financing its expansion scheme. The plant and machinery purchased for the project with the loan were not received during the year and those were still in transit at the end of the year. A sum of ₹ 4,000 was paid to a broker who arranged the loan. Discuss the admissibility of the interest.

Answer : Interest paid in respect of capital borrowed for the purposes of business or profession is admissible u/s 36(1)(iii). As per the Proviso to Sec. 36(1)(iii) inserted by the Finance Act, 2005, from assessment year 2006-2007, interest paid in respect of capital borrowed for acquiring an asset for extension of existing business or profession (whether capitalised in the books of account or not) for any period beginning from the date on which the capital is borrowed for acquisition of the asset till the date on which such asset is first put to use cannot be allowed as deduction. In this case, the asset has not been put to use till the end of the previous year. Therefore, interest of ₹ 50,000 is not be allowed as deduction. However, the cost of the asset is to be increased by the amount of interest and depreciation is admissible on enhanced cost [Proviso to Sec. 36(1)(iii)]. The deduction brokerage of ₹ 4,000 paid to a broker for arranging the loan there is a bit controversial

One view is that definition of the term “interest” u/s 2(28A) includes service fee or other charges in respect of monies borrowed, “brokerage” can be considered to fall under the scope of the term “other charges” and is therefore included under the definition of interest. Hence, brokerage of ₹ 4,000 for arranging the loan should be treated in the same way as interest. As per the other view, where brokerage or commission paid to an agent for arranging a loan for the purpose of business is not allowable as deduction u/s 36(1)(iii), but is allowable under Sec. 37(1). As per this view, ₹ 4,000 paid to a broker for arranging a loan is allowable as a deduction under Sec. 37(1).

Illustration 30 : Apporva Shantilal filed his return of income for the assessment year 2011-12 on 29-1-2012 showing a loss of ₹ 11,42,000. The same represented unabsorbed depreciation of foundry business of ₹ 9,00,000 and the balance loss in foundry business. During the previous year relevant to the assessment year 2012-13, two businesses are carried on by him – a steel rolling mill at Kanpur and a fertiliser manufacturing company at Cuttack. The foundry business was not carried on (discontinued). Separate books of account are being maintained for the two business carried on at different places. The following information is made available to you :

Relating to steel rolling mill at Kanpur

Particulars	₹
(a) Business Income prior to depreciation and following adjustments	5,60,000
(b) Opening WDV of factory building This building, constructed 5 years back, was sold for	6,20,000 10,28,000
(c) Machinery (entitled to depreciation @ 15%) Opening WDV All machines sold in March 2012 for	3,20,000 5,10,000
(d) Car Opening WDV	1,20,000

Relating to fertiliser unit at Cuttack

Particulars	₹
(a) Factory building (purchased in March, 2007) Opening WDV	2,80,000
(b) New Machinery (Rate of depreciation 15%) purchased in June, 2011	50,00,000
(c) Jeep Opening WDV	1,80,000
(d) Furniture Opening WDV	80,000
(e) Business income prior to above adjustments	7,16,000

Compute the total income of Mr. Apoorva Shantilal for the A.Y. 2012-13

Solution :

Computation of depreciation/short term capital gains in the case of Mr. Apoorva Shantilal for the A.Y. 2012-13 :

Particulars		₹
Profits and gains of business		
Profits prior to depreciation of steel rolling mill	5,60,000	
Profits prior to depreciation of fertiliser unit	7,16,000	
	<u>12,76,000</u>	
Depreciation for the year (Note - 1)	7,74,500	
	<u>5,01,500</u>	
Less : Set-off of Brought Forward Unabsorbed Depreciation u/s 31(2) – related	5,01,500	Nil
Capital Gains		
Short-term Capital Gain on Sale of Building (Note-1)	1,28,000	
Less : Set-off of Brought forward Unabsorbed Depreciation for the A.Y. 2011-12 restricted to the amount of profits	<u>1,28,000</u>	Nil
Gross Total Income		Nil
(-) Deduction under Chapter-VIA		Nil
Total Income		Nil

Note : The assessee can carry forward ₹ 4,08,500 being unabsorbed depreciation for set off against income in the future years.

Working Note :

1. Computation of Depreciation and Short Term Capital Gains

Particulars	Block-I	Block-II	Block-III	Block-IV
	Factory Building	Furniture & Fixture	Plant & Machinery	Moter Vehicles
Rate of Depreciation	10%	10%	15%	15%
Opening WDV				
— Kanpur	6,20,000	Nil	3,20,000	1,20,000
— Cuttack	2,80,000	80,000	Nil	1,80,000
Total opening WDV	9,00,000	80,000	53,20,000	3,00,000
Add : Additions during the year	Nil	Nil	50,00,000	Nil
	9,00,000	80,000	53,20,000	3,00,000
Less : Sales during the year	10,28,000	Nil	5,10,000	Nil
Short term Capital Gains	1,28,000	N/A	N/A	N/A
Net Book Value	Nil	80,000	48,10,000	3,00,000
Less : Depreciation for the year	Nil	8,000	7,21,500	45,000
Closing WDV	Nil	72,000	40,88,500	2,55,000
Total Depreciation	8,000 + 7,21,500 + 45,000 = 7,74,500			

2. Unabsorbed Depreciation – to be carried forward from Assessment Year 2011-12 ₹ 2,70,500 (after Set-off of ₹ 6,29,500 against income during the year) relating to Assessment Year 2012-13.

3. Unabsorbed Business loss of ₹ 2,42,000 (= ₹ 11,42,000 – 9,00,000) of A.Y : 2011-12 cannot be brought forward for setting off as the return of income for that Assessment Year was filed after due date of furnishing return u/s 139(1).

Illustration 31 : A firm comprising of four partners A, B, C and D carrying on business in partnership, sharing profits/losses equally shows a profit of ₹ 2,00,000 in its books after deduction of the following amounts for the year :

Particulars	₹
(a) Remuneration to partner 'A' who is not actively engaged in business	60,000
(b) Remuneration to partners 'B' & 'C' actively engaged in business	
Partner 'B'	80,000
Partner 'C'	90,000
(c) Interest to partner 'D' on loan of ₹ 1,50,000	36,000

The deed of partnership provides for the payment of above remuneration and interest to partners. You are required to work out the taxable income of the firm as well as partners for assessment year 2012-13.

Solution :

Computation of Income under the head Profits and Gains of Business or Profession

Particulars	₹
Net profit as per P/L A/c	2,00,000
Add : Inadmissible expenses —	
(i) Remuneration to A (not an active partner) – disallowed u/s 40(b)	60,000
(ii) Remuneration to B and C – (considered separately [₹ 80,000 + 90,000])	1,70,000
(iii) Interest paid to D on Loan advanced	36,000
Net Profit before Interest and Remuneration to Partners	4,66,000
Less : Maximum Permissible Interest u/s 40(b) @ 12% on Loan from D = ₹ 1,50,000 × 12% p.a.	18,000
Book Profit	4,48,000
Less : Maximum Permissible Remuneration to B and C u/s 40(b)	
(i) upto ₹ 3,00,000 – ₹ 1,50,000 or 90% of Book Profits, whichever is higher = 2,70,000 Balance of Book Profits – 60% of Book Profits = 60% of 1,48,000 = 88,800	3,58,000
(ii) Actual Remuneration paid lower of (i) & (ii), allowed as deduction	1,70,000
Taxable Income	2,78,000

Taxable income of the partners

Particulars	A	B	C	D
Remuneration	Nil	80,000	90,000	Nil
Interest	Nil	Nil	Nil	18,000
Taxable income	Nil	80,000	90,000	18,000

Working notes :

- (1) In the case of a firm, remuneration to a partner who is not a working partner is not eligible for deduction. In the case of working partners the remuneration paid is disallowed if it exceeds the limit prescribed u/s 40(b) with reference to “book profit”.

Book working partners remuneration is worked out as under :

	₹
First ₹ 3,00,000 of the book profit @ 90%	2,70,000
On the balance ₹ 1,98,000 of book profit @ 60%	1,18,800
Total	3,88,800

- (2) Any interest and salary to partners disallowed in the firm’s case shall not be included in the total income of the partner and shall not be chargeable to tax in the partner’s hands.
- (3) Share of profits of the partners is exempt u/s 10(2A) of the Income-tax Act and therefore, not included in the partner’s taxable income.



Illustration 32 : X Ltd., carrying on business in manufacture and sale of textiles, showed a net profit of ₹ 10,50,000 in its Profit and Loss Account for the period ending March 31, 2012. On the basis of the following particulars noted from the company's accounts and ascertained on enquiry, compute, giving reasons, the total income of the company for the assessment year 2012-13. The company maintains books of account on the basis of mercantile system.

1. The general reserve account shows a credit of ₹ 2,75,000 under the head "Surplus on devaluation". The enquiries show that the company had exported textile to U.S.A. during the year 1995-96. The sale proceeds were placed in a separate bank account in U.S.A. which were utilized for import of cotton from time to time. After obtaining permission from the Reserve Bank of India, in January 2012 the company remitted to India a sum of ₹ 2 lakh, being the balance standing to its credit in the said bank account which included the above surplus realized on account of devaluation of the rupee in June 1996. The company claims that the said surplus is not taxable, firstly, on the ground that the said surplus did not relate to the previous year and secondly, the said surplus is not a trading receipt.
2. The company had imported automatic looms under a special permission granted by the Textile Commissioner under the Cotton Textile (Control) Order, 1948. One of the conditions laid down while granting the permission was that the company should execute a bond in favour of President of India agreeing to export an agreed quantity of cloth and in default pay a sum calculated at the rate of 10 paise per metre to cover the shortfall. The company fell short of the target during the previous year as a result of which it was required to pay a sum of ₹ 40,000 towards the shortfall. The company has debited the said amount to "General expenses account".
3. The company has set up a laboratory for conducting research in textile technology. It has incurred a capital expenditure of ₹ 1,00,000 for the said purpose. The amount is shown in the balance sheet as "Laboratory equipment account" but is claimed as deduction in the return of income for the assessment year 2012-13.
4. The interest account includes payments amounting to ₹ 50,000 on deposits made by non-resident buyers of textile manufactured by the company. The said payments were made outside India without deduction of tax.
5. The legal charge includes a sum of ₹ 60,000 paid to solicitors for framing a scheme of amalgamation of all other textile mill with the assessee-company. The scheme is approved by the Central Government in public interest.
6. Travelling expenses include a sum of ₹ 1,25,000 being expenditure incurred by the directors of the company in connection with their tour to USA and UK for the purchase of new machinery for setting up a new plant for manufacture of caustic soda.
7. ₹ 1,00,000 (debited to profit and loss account) is paid to an approved Notional Laboratory with a specific direction that it shall be used for an approved scientific research programme.

Solution :

Computation of Income from Business

A. Y : 2012-13

	₹
Net profit as per Profit and Loss Account	10,50,000
<i>Adjustments :</i>	
Surplus arose on conversion of foreign currency into Indian currency (since foreign currency was kept for purchasing stock-in-trade, it will be revenue receipt)	(+) 2,75,000
Payment of ₹ 40,000 towards the shortfall in export (allowable as deduction since the payment is not penalty)	—
Capital expenditure on scientific research	(-) 1,00,000
Interest to non-residents [not deductible under section 40(a) since payment was made without deducting tax at source]	(+) 50,000
Legal charges for framing amalgamation scheme [deductible u/s 35DD in five years]	(+) 48,000
Travelling expenses of directors [section 37(1) does not permit a deduction of capital expenditure]	(+) 1,25,000
Weighted deduction under section 35(2AA) in respect of ₹ 1,00,000 paid to a National Laboratory [amount deductible is 200% of ₹ 1,00,000,	(-) 1,00,000
(-) Amount	1,25,000
Show in P/L A/c	1,00,000
Expenses not debited earlier	1,00,000
Net Income	13,48,400

Illustration 33 : D Ltd., carrying on business in manufacture, sale and export of tyres, tubes and accessories, has disclosed a net profit of ₹ 21,00,000 in its P & L account for the period ending March 31, 2012. On the basis of the following particulars furnished by the company and ascertained on inquiry, compute, giving reasons, its total income for the assessment year 2012-13. The company follows the mercantile system of accounting :

- (a) A sum of ₹ 20,000 is debited to compensation account. The company had placed an order for machinery to manufacture tyres with a UK company. However, due to a sudden increase in the price of machinery by the vendor, the assessee, had to cancel the contract, in lieu of compensation. The company claims the said amount as deduction on revenue account or, in the alternate, as loss under the head "Capital gains" as the payment was made towards extinguishment of right to acquire a capital asset.
- (b) "Loss on export of accessories account" shows a debit of ₹ 4 lakh. In this connection it is explained that two trucks belonging to the company carrying tyres accessories were intercepted at the international border and seized by customs authorities for illegal export. The goods were confiscated by the customs authorities and a fine of ₹ 2 lakh was levied. The company claims the value of confiscated goods as a trading loss under section 28 and the payment of the fine of ₹ 2 lakh which is debited to rates and taxes account as on expenditure in the course of business under section 37(1).
- (c) The company had set up a separate unit for manufacture of plastic tubes at Bangalore in 1996. The said unit suffered heavy losses. As a result the same was closed down and the plant and machinery were sold away. The company, however, claims unabsorbed depreciation amounting to ₹ 8 lakh in its return of income. It is not debited to the profit and loss account.
- (d) During the previous year 1996-97, the assessee-company acquired 5,000 shares of E Ltd., an Indian company, as a result, the entire share capital of the said company is now held by the assessee-company. In May 2011, the assessee-company sold to E Ltd. plant and machinery for ₹ 6,00,000. The actual cost is ascertained at ₹ 4,00,000 and written down value at ₹ 1,50,000.
- (e) In the years 2001-2002 and 2002-03, the Government of India arranged exports of tyres and tubes through the Federation of Tyre Dealers of which the company was a member. The exports which were made to Far Eastern countries resulted in loss which was shared by all members including the company. The Federation thereafter took up the questions of reimbursement of losses with the Government, which after protracted discussion and correspondence agreed to grant a subsidy calculated at a certain percentage of exports. The assessee-company received its share of subsidy amounting to ₹ 3 lakh in the previous year. The amount stands credited to the "Capital reserve account" and claimed as exempt.

Solution :

Computation of Total Income for A.Y. 2012-13

	₹
Net profit as per Profit and Loss Account	21,00,000
<i>Adjustments :</i>	
(i) Payment of compensation [not allowable since payment is in the nature of capital expenditure, being made to avoid unnecessary investment in capital asset ; nor can it be allowed as capital loss as there is no transfer of capital asset]	(+) 20,000
(ii) Loss arising out of confiscation of stock by customs authorities [not deductible by virtue of Explanation to section 37(1)]	(+) 4,00,000
(iii) Fine [not allowable as penalty paid for breach of law is not normal incidence of business]	(+) 2,00,000
(iv) Unabsorbed depreciation of a unit closed before the commencement of previous year [allowable as deduction]	(-) 8,00,000
(v) Recovery of loss [taxable under section 41 (1)]	(+) 3,00,000



(vi) Compensation paid on voluntary retirement of employees [under section 35DDA, one-fifth of such compensation is deductible in the year in which the expenditure is incurred and the balance is deductible in the next four years; section 35DDA is applicable even if the voluntary retirement scheme has not been framed in accordance with the guidelines given under section 10(10C);	(+) 22,40,000
$\left[28,00,000 - \frac{1}{5} \times 28,00,000 \right]$	
Business Profit	44,60,000
Capital gain on sale of machinery to wholly owned subsidiary company [since transferee-company is wholly owned Indian subsidiary company of the assessee, the transaction is not treated as transfer under section 47(iv) and surplus arising on transfer is not taxable as capital gain]	—
Net Income	44,60,000

Illustration 34 : Bharat, owner of Great India Roadways, furnishes following details for the A.Y. 2012-13.

	₹
Revenue from customers	31,00,000
Less : Expenses	
Rent of office premises	1,80,000
Rent of godown	2,40,000
Truck Driver salary	5,00,000
Allowance to truck driver	1,20,000
Cost of petrol, diesel, etc	7,50,000
Other expenses other than depreciation	2,00,000
Income from business without charging depreciation	11,10,000

Additional Information :

Great India Roadways have following details of its assets —

Assets	Written down value as on 1.4.2011
Office Premises	₹ 2,50,000
Machinery block (30%) consists of —	₹ 20,00,000
— 2 Diesel engine trucks of 13000 kgs each	
— 2 Diesel engine trucks of 10000 kgs each	
— 1 Petrol engine truck of 12000 kgs	

During the year, he purchased 2 medium-size-truck (petrol engine) for ₹ 3,50,000 each on 13.7.2010. However, one petrol engine truck of 12,000 kgs was sold on 9.9.2011 for ₹ 1,00,000.

Compute his income under the head Profits & gains of business or profession.

Solution :

Computation of Profits & gains of business or profession of Shri Bharat for the A.Y. 2012-13

Particulars	Amount
Net profit as per Profit and Loss A/c	11,10,000
Less : Expenditure allowed but not debited to P & L A/c	
Depreciation u/s 32 (Note)	8,05,000
Profits & gains of business or profession	3,05,000

Note : Computation of depreciation allowed u/s 32

Particulars	Details	Amount
Block 1 : Office Premises @ 10% W.D.V. as on 1.4.2011 <i>Add</i> : Purchase during the year <i>Less</i> : Sale during the year Depreciation @ 10% on ₹ 2,50,000	2,50,000 Nil 2,50,000 Nil 2,50,000	25,000
Block 2 : Trucks @ 30% W.D.V. as on 1.4.2011 <i>Add</i> : Purchase during the year <i>Less</i> : Sale during the year Depreciation @ 30% on ₹ 26,00,000 Depreciation allowed u/s 32	20,00,000 7,00,000 27,00,000 1,00,000 26,00,000	7,80,000 8,05,000

Alternative II : Computation of income u/s 44AE

No. of vehicle	Type of goods carriage	Month including part of month	Details	Income ₹
2 Diesel engine trucks of 13000 kgs each	Heavy	12	3500×12×2	84,000
2 Diesel engine trucks of 10000 kgs each	Other vehicle	12	3150×12×2	75,600
1 Petrol engine truck of 12000 kg	Other vehicle	6	3150×6×1	18,900
2 medium size truck	Other vehicle	9	3150×9×2	56,700
Profit and gains of business or profession				2,35,200

Income of the assessee under the head Profits & gains of business or profession shall be ₹ 2,35,200 u/s 44AE.

Illustration 35 : During the previous year 2011-12, profit and loss account of Shri Amarnath, proprietor of Free Bird Enterprises engaged in the business of dymade garments, shows profits of ₹ 4,50,000. With the following information, compute his taxable income from business -

- Interest on capital ₹ 5,000
- Purchases include goods of ₹ 42,000 from his younger brother in cash. However, market value of such goods is ₹ 35,000.
- Interest paid outside India ₹ 1,00,000 without deducting tax at source.
- Penalty paid to local government for non-filing of sales tax return ₹ 5,000
- Penalty paid to customer for non-fulfilling of order within time ₹ 10,000
- Bad debts ₹ 1,00,000. Money has been advanced for purchase of Building.
- Revenue expenditure on promoting family planning among employees ₹ 10,000.
- Premium paid on health of employees ₹ 6,000 in cash
- Premium paid on health of his relatives ₹ 6,000 in cheque
- Employer's contribution to RPF ₹ 12,000. One-half of the amount is paid after due date as per relevant Act but before 31.3.2011



- (k) Employees contribution to RPF ₹ 10,000. ½ of the amount is paid after due date as per relevant Act.
- (l) Interest on late payment of sales tax ₹ 1,000 (yet to be paid)
- (m) Interest on loan from State Bank of India ₹10,000 (₹ 5,000 is not paid till due date of filing of return)
- (n) Interest on late refund from income tax department ₹ 500
- (o) Sale includes sale to Raj ₹ 10,000. (Cost of such goods ₹ 8,000; Market value of such goods ₹ 12,000)
- (p) He received ₹ 80,000 from a debtor at a time in cash.
- (q) Recovery of bad debt ₹10,000 (out of which ₹ 8,000 was allowed as deduction during AY. 2007-08)
- (r) Depreciation (being not debited in accounts) ₹ 20,000 allowed as deduction u/s 32

Solution :

Computation of Profits and gains of business or profession of Shri Amarnath for the AY. 2012-13

Particulars	Note	Details	Amount
Net profit as per Profit and Loss account			4,50,000
Add : Expenditure disallowed but debited in P & L A/c			
Interest on capital	1	15,000	
Payment to relative in excess of market value of goods	2	7,000	
Interest paid outside India without deducting tax at source	3	1,00,000	
Penalty paid to local government for non-filing of sales tax return	4	5,000	
Bad debt	6	10,00,000	
Premium paid on health of employees in cash	8	6,000	
Premium paid on health of his relatives in cheque	9	6,000	
Employees contribution to RPF	11	5,000	
Interest on loan from State Bank of India	13	5,000	
Cost of goods sold to himself	14	8,000	2,43,000
			<u>3,93,000</u>
Less : Expenditure allowed but not debited in P & L A/c			
Depreciation u/s 32		20,000	
Less : Income not taxable but credited to P & L A/c			
Sales to himself (goods withdrawn for personal purpose)	14	10,000	
Recovery of bad debts	15	2,000	
Less : Income taxable under other head but credited to P & L A/c			
Interest on late refund from income tax department	16	500	32,500
Profits and gains of business or profession			<u><u>3,60,500</u></u>

Notes :

- (1) Interest on capital to proprietor is not allowed as no one can earn from a transaction with himself. The provider of loan and receiver of loan are same hence does not involve any actual expenses.
- (2) Any unreasonable payment to relative is disallowed u/s 40A(2). Hence, ₹3,000 is disallowed. Since cash payment towards allowed expenditure (i.e. ₹19,000) does not exceed ₹ 20,000, hence provision of sec. 40A(3) is not applicable.
- (3) Any salary paid outside India without deducting tax at source is disallowed u/s 40(a).
- (4) Any payment made for infringement of law is disallowed.
- (5) Payment made for non-fulfilling of contract is not a payment for infringement of law Hence, allowed u/s 37(1).

- (6) Bad debt is allowed only when such debt has been taken into account as income of previous year or any earlier previous year(s) [Sec. 36(1)(vii)]. Since, the debt is in respect of purchase of a building, which was not considered as income of any previous year, hence it is disallowed.
- (7) Any expenditure for promoting family planning is allowed to company assessee [Sec. 36(1)(ix)]. However, such expenditure (revenue in nature) incurred by assessee other than company shall be allowed u/s 37(1).
- (8) Payment of insurance premium on health of employees in cheque is allowed u/s 36(1)(ib).
- (9) Payment of insurance premium on health of relative is not related to business, hence disallowed.
- (10) Employer's contribution towards RPF is allowed if payment is made before due date of filing of return irrespective of fact that such payment was made after due date prescribed in the relevant Act.
- (11) Any sum received from employees as their contribution towards RPF is allowed only when such sum has been credited to such fund within the due date prescribed in the relevant Act [Sec. 36(1)(va)].
- (12) Interest on late payment of sales tax is not a penalty but compensatory in nature. Hence, it is allowed u/s 37(1) Further such interest is not governed by the provisions of sec. 43B.
- (13) Any interest payable to any scheduled bank is allowed on cash basis [Sec. 43B]. Hence, unpaid amount is disallowed.
- (14) Any expenditure of personal nature is not allowed. Further, no one can earn from a transaction with himself. Hence, sale made to himself is not treated as income.
- (15) Bad debt recovery is treated as income in the year of recovery to the extent of bad debt allowed in the earlier year [Sec. 41(4)]
- (16) Interest on late refund of income tax is taxable under the head 'Income from other sources'.
- (17) Receipt from debtor ₹ 80,000 in cash is not attracted by provision of sec. 40A(3).

Illustration 36 : Discuss the admissibility or otherwise of any five of the following claims in connection with assessment to income-tax. They do not necessarily relate to the same assessee:

- (i) An expenditure of ₹ 1,00,000 was incurred on the occasion of the silver jubilee of the company for presentation of silver mementos to shareholders and directors, the value of each memento being ₹ 1,000 only.
- (ii) An assessee carries on business in respect of which it holds tenancy rights. It carries out improvements to the said building at a cost of ₹ 2,00,000 and claims depreciation @ 10% thereon. The assessing officer rejects the claim on the ground that the assessee is not the owner of the building.
- (iii) Excise duty amounting to ₹ 2,00,000 for the period 2010-11 was paid by the company by 30-9-2011 before furnishing the return of income for the assessment year 2011-12.
- (iv) A criminal case was filed against a company under the Essential Commodities Act, 1955. The company incurred litigation expenses amounting to ₹ 50,000 to defend the directors. The directors were ultimately acquitted.
- (v) A company was generating electricity privately for its factory. Later, at its expense, electric lines were laid from the trunk road to the factory. It paid ₹ 5,00,000 to the State Electricity Board as its contribution for this purpose. The ownership of the power-line was to vest with the State Electricity Board.
- (vi) X and Y are two shareholders of Pooja Ltd., a closely held company. X holds 55% share capital on 30-1-2011, X transfers his shares to A. Pooja Ltd. wants to set off brought forward loss of ₹ 4,00,000 (business loss ₹ 1,00,000; unadjusted depreciation ₹ 3,00,000) of the previous year 2009-10 against the income of the previous year 2010-11 (i.e., ₹ 9,00,000). Can it do so?

Solution :

- (i) As per the decision of the Apex Court in the case of *Aluminum Corporation of India Ltd. v CIT* (1972) 86 ITR 11 (SC) and various other decisions, where an expenditure is incurred for commercial expediency, the same shall be allowed as deduction under section 37(1). If at the time the expenditure is incurred, commercial expediency justifies it, it will be taken to be for the purpose of the business even though not supported by any prevailing practice.

Presentation of silver mementos to the directors and shareholders on the occasion of silver jubilee is to motivate both the directors and the shareholders. The expenditure has been incurred on account of commercial expediency and should qualify for deduction under section 37(1).



- (ii) According to Explanation to section 32(1) where the business or profession of the assessee is carried on in a building not owned by him but in respect of which the assessee holds a lease or other right of occupancy and any capital expenditure is incurred by the assessee for the purposes of the business or profession on the construction of any structure or doing of any work, in or in relation to, and by way of renovation or extension of, or improvement to, the building, then, the provisions of section 32 shall apply as if the said structure or work is a building owned by the assessee. Hence, depreciation in this case will be allowable.
- (iii) As the excise duty has been paid or before the due date of furnishing return under section 139(1) in respect of the previous year in which the liability to pay such sum was incurred, the same shall be allowed as deduction on due basis as per section 43B.
- (iv) Section 37(1) does not make any distinction between expenditure incurred in civil litigation and that incurred in criminal litigation. All that the court has to see is whether the legal expenses were incurred by the assessee in his character as a trader, in other words, whether the transaction in respect of which proceedings are taken arose out of and was incidental to assessee's business. Further, it is to be seen whether the expenditure was *bona fide* incurred wholly and exclusively for the purpose of the business. [*CIT v Birla Cotton Spg. & Wvg. Mills Ltd.* (1971) 82 ITR 166 (SC)]. In view of this, the litigation expenses of ₹ 50,000 incurred in detending directors is deductible under section 37(1).
- (v) The new electric power lines were laid to run the factory efficiently but since the ownership of the power lines was to vest with the State Electricity Board, the contribution of ₹ 5,00,000 paid to the State Electricity Board shall be allowable as revenue expenditure under section 37(1).
- (vi) According to section 79 the losses of a closely held company can be carried forward and set off in the subsequent assessment year only when at least 51% of the shares of the company carrying voting rights are held by the same persons as on the last day of the previous year in which the loss was incurred and the last day of the previous year in which the losses are set off. In this case business loss will not be allowed to be set off but unabsorbed depreciation is not a loss and shall be allowed to be set off.

Illustration 37 : Discuss the correctness or otherwise of the following propositions with reasons therefor :

- (a) Where a person draws from his own stock-in-trade for personal use, there can be no taxable profit.
- (b) Even an outlay for acquiring an enduring advantage for business may be deductible as revenue expenditure.

Solution :

- (a) The Supreme Court in *CIT v. Kikabhai Premchand* (1953) 24 ITR 506 held that when a person draws from his own stock-in-trade for personal use, there can be no taxable profit as in this case the vendor and the vendee are not different. To constitute a sale these should be one buyer and seller. The buyer and seller has to be different entity to constitute a proper sale.
- (b) Normally, an amount spent for acquiring an enduring advantage for business is of capital nature but there can be certain cases when the amount spent on acquiring an enduring advantage may be treated as revenue expenditure. The Supreme Court in *CIT v. Empire Jute Co. Ltd.* (1980) 124 ITR 1 held that when a jute mill as a result of an arrangement with other jute mill had undertaken to work only for specified hours during a week but exceeded the same and paid for such excess period to other members of the pooling arrangement, such payment is known as purchasing loom hours. Though looms are capital assets, the payment was for their operations. By the purchase of loom hours no new asset was created and there was no addition to or expansion of the profit-making apparatus of the company. Hence, such payment is of revenue nature.

Illustration 38 : A Public Limited Company engaged in the generation and distribution of power had its business acquired by the Government in June 2009. Certain items of plant and machinery used by the Company in its business were taken over by the Government at a price which resulted in the Company realizing a surplus of ₹ 26,60,000 over its written down value. The compensation was received by the Company in April 2010 which was accepted by it under protest. The Company proceeded to initiate arbitration proceedings under law and was granted an additional compensation of ₹ 16 Lakhs. This was decided by the arbitrators in December 2009 and received by the Company in March 2011.

The Company claims that the assessment of the Company to tax should not be made since the business was completely taken over by the Government in June 2009 and at the time of final determination of compensation in March 2011, the Company did not exist.

Do you agree to the Company's claim? Discuss with reference to the Assessment Year(s) to which the claim to tax, if any, can be related.

Solution :

1. In case of acquisition of property under any law, the balancing charge u/s 41(2) is taxable as income of the previous year in which it becomes due and not in the year in which it was settled. [United Provinces Electric Supply Co. 110 Taxman 134 (SC)]
2. As per Explanation to Section 41(2), even when the business is not in existence, such balancing charge shall be taxable in its hands as if it is in existence in the relevant previous year.
3. **Conclusion :**
 - (a) Surplus of ₹ 26,60,000 — taxable in A.Y. 2010-11 as Balancing Charge under the Business Income.
 - (b) Additional Compensation of ₹16,00,000 determined in December 2010 taxable as Balancing Charge in AY 2011-2012 under Business Income.

Illustration 30 : Mr. Tony has estates in Rubber, Tea and Coffee. He derives income from them. He has also a nursery wherein he grows plants and sells. For the previous year ending 31.3.2012, he furnishes the following particulars of his sources of income from estates and sale of Plants. You are requested to compute the taxable income for the Assessment year 2012-2013.

(a) Manufacture of Rubber	₹ 5,00,000
(b) Manufacture of Coffee grown and cured	₹ 3,50,000
(c) Manufacture of Tea	₹ 7,00,000
(d) Sale of Plants from Nursery	₹ 1,00,000

Assessee : Mr. Tony

Previous Year : 2011-12

Assessment Year : 2012-2013

From the words 'Mr. Tony has estates', it is presumed that he had grown Tea, Coffee and Rubber, and also Plants in his Estates, and the amount given is the Profits of the Business.

Computation of Taxable Income is as under —

Particulars	Agricultural Income	Non-Agricultural Income
Growing and Manufacture of Rubber [Rule 7A]	$5,00,000 \times 65\% = ₹ 3,25,000$	$5,00,000 \times 35\% = ₹ 1,75,000$
Grown and Cured Coffee [Rule 7B]	$3,50,000 \times 75\% = ₹ 2,62,500$	$3,50,000 \times 25\% = ₹ 87,500$
Growing and Manufactured of Tea [Rule 8]	$7,00,000 \times 60\% = ₹ 4,20,000$	$7,00,000 \times 40\% = ₹ 2,80,000$
Growing & Sale of Plant by Nursery [See Note]	₹ 1,00,000	—
Total	₹ 11,07,500	₹ 5,42,500
Taxable Income	Exempt u/s 10(1)	₹ 5,42,500



STUDY NOTE - 7

CAPITAL GAINS

This Study Note includes

- Charging Section
- Provision for computation of capital gains and related exemptions

7.1 CHARGING SECTION: 45(1)

Any profits or gains arising from transfer of any capital asset shall be chargeable to income-tax as Capital Gains and shall be deemed to be the income of the previous year in which the transfer took place.

7.2 PROVISION FOR COMPUTATION OF CAPITAL GAINS AND RELATED EXEMPTIONS

1. Capital Asset: [Section 2(14)]

Includes :

Property of any kind, whether or not connected with business or profession

Excludes :

- Stock in trade
- Personal Effects
- Rural Agricultural Lands in India
- 6 ½ % Gold Bonds 1977; 7% Gold Bonds 1980 & National Defence Gold Bonds, 1980.
- Special Bearer Bonds, 1991
- Gold Deposit Bonds issued under Gold Deposit Scheme 1999

N.B: Items (d) and (e) instruments do not exist now; they are only for academic significance. For the above purpose:

- Stock in Trade means:** Raw material or Consumable stores used by the assessee In his business or profession.
- W.e.f. A.Y. 2008-09, Personal effect means** Movable property Including wearing apparel and furniture held for personal use by the assessee or any member of his family dependent on him but excludes:
 - Jewellery
 - Archaeological collections
 - Drawings
 - Paintings
 - Sculptures or
 - Any work of art.

2. Short-term Capital Asset (STCA) [Section 2(42A)]

- For all Capital Assets other than financial assets:** Capital assets held by an assessee for not more than 36 months Immediately preceding the date of transfer are treated as short-term capital assets.
- For Financial Assets:**
Equity (or) Preference shares of a company, Unit of UTI or unit of Mutual Fund u/s 10(23D), Securities listed in a recognized stock exchange, Zero Coupon Bonds treated as STCA if they are not held for more than 12 months.

3. Long-term Capital Asset (LTCA) [Section 2(29A)] - Not a short-term capital asset.

4. Capital Gains:

- Long-term Capital Gain [Section 2(29B)]** - Capital Gain arising from transfer of Long Term Capital asset.

- (b) **Short-term Capital Gain [Section 2(42B)]** - Capital Gain arising from transfer of Short Term Capital Asset.

5. Zero Coupon Bond [Section 2(48)]

a. Zero Coupon Bond means a bond —

- (i) **Issued By:** (I) Any Infrastructure Capital Company, or (ii) Infrastructure Capital Fund, or (iii) Public Sector Company.
- (ii) **Issue Date:** On or after 01.06.2006.
- (iii) **Payment/Benefit:** No payment and benefit is received or receivable before maturity or redemption from Infrastructure Capital Company / Infrastructure Capital Fund / Public Sector Company, and
- (iv) **Notified by Central Government:** The Central Government may, by notification in the Official Gazette, specify in the behalf.

b. **Treatment in the hands of Issuer u/s 36(1) (iiia) :** Discount on **Zero Coupon Bonds**.

- (i) Is the difference between Maturity / Redemption Value and the issue price.
- (ii) Can be written off on a pro-rata basis over the period of the bond.

c. **Treatment in the hands of Investor:**

- (i) **Financial Asset:** Zero Coupon Bond is a Financial Asset for the purpose of Capital Gains.
- (ii) **Taxability:** Transfer or Maturity of Zero Coupon Bond will be taxable as Capital Gains.

6. Infrastructure Capital Company and Infrastructure Capital Fund for the purpose of Zero Coupon Bonds.

- a) **Infrastructure Capital Company [Sec.2 (26A)] :** It is a Company which makes investment by way of acquiring shares or providing long-term finance to any prescribed enterprise or undertaking.
- b) **Infrastructure Capital Fund [Sec.2 (26B)] :** It is a Fund operating under a Trust Deed established to raise monies by Trustee for investment by way of acquiring shares or providing long-term finance to any prescribed enterprise or undertaking.
- c) **Prescribed Undertaking/Enterprise :**
 - (i) Enterprise/Undertaking wholly engaged in the infrastructure business referred in Sec. 80-IA/80-IAB, or
 - (ii) Housing Projects referred in Section 80-IB, or
 - (iii) Project for constructing a Hotel (at least of 3 Star Category) or Hospital with one hundred beds for patients.

7. Transfer u/s 2 (47)

Sec 2(47)	Nature of Transaction
(i)	Sale, exchange, relinquishment
(ii)	Extinguishment of any rights in an asset
(iii)	Compulsory acquisition thereof under any law
(iv)	Conversion of capital asset into stock-in-trade
(iva)	Maturity/Redemption of a Zero Coupon Bond
(v)	Part performance of a Contract u/s 53A of the Transfer of Property Act of possession of property
(vi)	Transactions, which have the effect of transferring/enabling the enjoyment of immovable property.

Sale: As per Sec. 54 of the Transfer of Property Act, "Sale is a transfer of ownership in exchange for a price paid or promised or part-paid and part promised".

Exchange: As per the Transfer of Property Act, 1882, when two persons mutually transfer the ownership of one thing for the ownership of another, neither thing or both things being money only, the transaction, is called an exchange.

Relinquishment: Relinquishment means withdrawn from, abandoning or giving up anything. Where an assessee gives up the right to claim specific performance for purchase of immoveable property it is relinquishment of a capital-asset.



Extinguishment or any rights in an asset: It means total destruction, annihilation, termination or extinction of a capital asset. It refers to extinguishment of rights on account of transfer (Vania Silk Mills Ltd.)

8. Indexed Cost of Acquisition (ICA) and Indexed Cost of Improvement (ICI) [Section 48]

When asset is acquired by assessee himself

- (a) **Acquired prior to 1.4.1981**

Indexed Cost Acquisition

Fair Market Value on 01.04.1981 or cost of acquisition whichever is high \times Cost of Inflation Index for the year of transfer/100.

- (b) **Acquired after 1.4.1981,**

$$\text{Indexed cost of Acquisition} = \frac{\text{Cost of Acquisition} \times \text{CII for year of transfer}}{\text{CII for year of acquisition}}$$

Indexed Cost of Improvement in both the above cases

$$= \frac{\text{Cost of Improvement} \times \text{CII for year of transfer}}{\text{CII for year of Improvement}}$$

ICI can be computed **only if it is incurred after 01.04.1981.**

When assessee received the asset u/s 47

- (c) **Asset acquired prior to 1.4.1981 by previous owner and received by the assessee prior to 1.4.1981.**

ICA = FMV on 1.4.81 or Cost of acquisition by previous owner whichever is high \times CII for year of transfer/100.

- (d) **Asset acquired prior to 1.4.81 by previous owner and received by the assessee after 1.4.81.**

ICA = FMV on 1.4.81 or Cost of acquisition by previous owner whichever is high \times cn for Year of transfer/ CII of year in which it is **first held by the assessee.**

- (e) **Asset acquired after 1.4.1981 by previous owner and received by assessee after 1.4.1981.**

$$\text{Indexed Cost of Acquisition} = \frac{\text{Cost of acquisition to the previous owner} \times \text{CII for year of transfer}}{\text{CII of year in which the asset is first held by the assessee}}$$

In the above cases: Indexed Cost of Improvement = Cost of improvement \times CII for year of transfer/ cn for year of improvement.

9. List the circumstances in which benefit of indexation is not available

Nature of LTCA Transferred	Assessee Not Eligible for
Bonds/Debentures except Capital Indexed Bonds Issued by Govt.	All Assesses
Shares/Debentures of Indian Company acquired by using Convertible Forex under First Proviso to Section 48	Non-Residents
Depreciable Assets	All Assesses
Slump Sale	All Assesses
Units Purchased in Foreign Currency u/s 115AB	Off Shore Fund
GDRs purchased in Foreign Currency u/s 115AC Individual	Non-Residents and Resident
Securites u/s 115AD	Foreign Institutional Investors.
Foreign Exchange Asset u/s 1150	Non-Resident Indian

10. Cost Inflation Index as notified by the Central Government is as under:

Financial Year	Cost inflation Index (CII)	Financial Year	Cost Inflation Index (CII)	Financial Year	Cost Inflation Index (CII)
1981-1982	100	1992-1993	223	2003-2004	463
1982-1983	109	1993-1994	244	2004-2005	480
1983-1984	116	1994-1995	259	2005-2006	497
1984-1985	125	1995-1996	281	2006-2007	519
1985-1986	133	1996-1997	305	2007-2008	551
1986-1987	140	1997-1998	331	2008-2009	582
1987-1988	150	1998-1999	351	2009-2010	632
1988-1989	161	1999-2000	389	2010-2011	711
1989-1990	172	2000-2001	406	2011-2012	785
1990-1991	182	2001-2002	426		
1991-1992	199	2002-2003	447		

11. EXCEPTIONS TO TRANSFER u/s 46 & 47

Section	Nature of transaction not considered as a Transfer
46(1)	Distribution of a capital asset in specie on liquidation of a company by a liquidator to its shareholders is not a transfer.
47(i)	Any distribution of capital assets on the total or partial partition of a HUF.
47(iii)	Any transfer of a capital asset under a gift or will or an irrevocable trust. Exception is also applicable In case of shares or securities received by employees from the company free of cost or at a concessional rate. However, a provision has been added to provide that this clause shall not apply to transfer under a gift or an irrevocable trust of a capital asset being shares, debentures or warrants allotted by a company directly or Indirectly to its employees under ESOS or ESOP of the company offered to such employees in accordance with the guidelines Issued by the Central Government in this behalf.
47(iv)	Transfer of any capital asset by a holding company to Its 100% subsidiary company which is an Indian company.
47(v)	When a transfer has been made by a 100% subsidiary to its Indian holding company. Both the sections 47(iv) and (v) are subject to the restrictive conditions imposed u/s 47A(1), which is as follows: (a) If within the course of 8 years from the date of transfer, holding company loses Its 100% stake on the subsidiary company. (b) If the transferee company transfers this capital asset as their stock-in-trade within 8 Years. In both the above cases, the earlier exemption so granted shall be withdrawn and there would arise incidence of capital gains, in the original year of transfer, which would be initiated as per Sec.155 (7B) amendment proceedings.
47(vi)	Transfer of a capital asset in a scheme of amalgamation where the amalgamated company is an Indian company. The conditions of Sec.2(1B) of the Act, must be fulfilled: (a) All the property and liabilities of the amalgamating company or companies immediately before the amalgamation becomes the property of the amalgamated company by virtue of amalgamation. (b) Shareholders holding not less than 75% in the value of shares in amalgamating company or companies (other than shares held therein immediately before the amalgamation or by a nominee for the amalgamated company or its subsidiary) become shareholders of the amalgamated company by virtue of amalgamation.

	Amalgamation as per income-tax includes merger and absorption, provided the conditions of sec.2 (1B) are satisfied.
47(via)	Transfer of shares of an Indian company by an amalgamated foreign company to a foreign amalgamated company, provided the following conditions are satisfied : (a) The transfer of shares is under a scheme of amalgamation between two foreign companies; (b) At least 25% of the shareholders of the amalgamating foreign company continue to remain shareholders of the amalgamated foreign company; (c) No tax is levied on such capital gain in the country where foreign amalgamating company is Incorporated.
47(viaa)	Transfer of capital asset by a banking company to a banking institution in a scheme of amalgamation sanctioned by the Central Government u/s 45(7) of the Banking Act 1949.
47(vib)	Transfer of a capital asset by the Demerged Company to the Resulting Indian company, subject to : the fulfillment of the following conditions : (a) Transfer of capital asset should be from demerged company to a resulting company; (b) Resulting company should be an Indian company; (c) Transfer of capital asset should be made in a scheme of demerger.
47(vic)	Transfer of shares of Indian company by a demerged foreign company in a demerger to a foreign company, shall not be treated as transfer provided the following conditions are fulfilled : (a) The shareholders holding not less than 75% in value of shares of the demerged foreign company continue to remain shareholders of the resulting foreign company; and (b) No tax is levied on capital gain in the foreign country in which the demerged company is Incorporated. The provisions of Sections 391 to 394 of the Companies Act, 1956 shall not apply in case of demergers referred in this clause.
47(vica)	Any transfer in a business reorganization, of a capital asset by the predecessor co-operative bank to the successor co-operative bank.
47(vicb)	Any transfer by a shareholder, in 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 allotment to him of any share or shares in the successor co-operative bank.
47(vid)	Transfer/allotment of shares by the resulting company to the shareholders of the demerged company in a scheme of demerger. Only shares must be exchanged against shares.
47(vii)	Allotment of shares in amalgamated company to the shareholders of amalgamating company, will not be considered as a transfer if : (a) The transfer is made in consideration of allotment to him of any share or share in the amalgamated company; and (b) The amalgamated company is an Indian company.
47(viia)	Transfer of shares/bonds or Global Depository Receipts (GDRs) referred to in Section 115AC (1), i.e., those bonds, shares or GDRs of a public company (being an Indian company) is purchased in foreign currency, outside India by a non-resident to another non-resident.
47(viii)	Transfer of urban agricultural land in India effected before 1.3.1970
47(ix)	Transfer of a capital asset being a work of art, archaeological, scientific or art collection, book, manuscript, drawing, painting, photograph or print to Government or University or National Museum or National Art Gallery, National Archives or any 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(x)	Conversion of bonds or debentures, debentures-stock or deposit certificates in any form, of a company into shares or debentures of that company
47(xi)	Transfer of membership of a recognized stock exchange in India by a person (not being a company) on or before 31st December 1998, to a company in exchange of shares allotted by that company, subject to the restrictions of Sec.47A(2)

47(xii)	<p>Transfer of capital asset being 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 worker's co-operative.</p> <p>Transfer should be made during the period commencing from the previous year in which the said company has become a sick industrial company u/s 17(1) of the Act and ending with the previous year during which the entire net worth of such company become equal to or exceeds the <u>accumulated losses</u>.</p>
47(xiii)	<p>Transfer of capital assets or intangible assets or any transfer of capital asset in the course of demutualization or corporatisation of a recognized stock exchange in India, on succession of a firm concern by a company, provided the following conditions are fulfilled :</p> <ol style="list-style-type: none"> All the assets and liabilities of the erstwhile firm or AOP/BOI, relating to the business immediately before succession becomes the assets and liabilities of the company; All the partners of the firm before the succession becomes 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; The partners are not in receipt of any other benefit, whether directly or Indirectly, in any form or manner, other than by way of allotment of shares in the company; 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; Their shareholding continues for a period of 5 years from the date of the succession; The demutualization or corporatisation of a recognized stock exchange in India is carried out in accordance with a scheme of corporatisation which is approved by SEBI.
47(xiiia)	<p>Transfer of a capital asset being a membership right held by a member of a recognized stock exchange in India for acquisition of shares and trading or clearing rights acquired by such member in that recognized stock exchange in accordance with a scheme of demutualization or corporatisation which is approved by SEBI.</p>
47(xiv)	<p>Transfer of capital asset or Intangible assets where a sole proprietary concern is succeeded by a company, provided the following conditions are fulfilled:</p> <ol style="list-style-type: none"> All the assets and liabilities of the erstwhile sole proprietary concern, relating to the business immediately before succession becomes the assets and liabilities of the company; The sole proprietor is not in receipt of any other benefit, whether directly or indirectly, in any form or manner, other than by way of allotment of shares in the company; The shareholding of the sole proprietor in the company is not less than 50% of the total voting power in the company; His shareholding continues for a period of 5 years from the date of the succession;
47(xv)	<p>Any transfer under the Securities Lending Scheme, 1997 for lending of any securities under an agreement or arrangement, between the assessee and borrower of securities as per the guidelines issued by SEBI or RBI.</p>

12. COST OF ACQUISITION u/s 55(2)

- The price paid by the assessee for the acquisition of the asset.
- Expenses incurred for completing the title is included in the cost of the asset.
- Expenses incurred in acquiring the asset or acquiring better voting rights
- Interest on capital borrowed for acquiring capital asset (however, expenditure incurred for acquiring loan amount for acquiring capital asset is not a part of cost of acquisition)
- Amount paid for discharge of mortgage, where the asset was mortgaged by the previous owner.
- Extra amount paid by coparcener for full ownership in specific property allotted to him by HUF



13. DEEMED COST OF ACQUISITION

- a) **Cost to the Previous owner u/s 49 (1):** where the capital asset became property of the assessee, the cost of acquisition of the asset shall be deemed to be cost for which the previous owner of the property acquired it, in the following cases:
- (i) on the distribution of assets on total or partial partition of HUF;
 - (ii) under a gift or will;
 - (iii) by succession, inheritance or devolution;
 - (iv) distribution of assets on the liquidation of a company;
 - (v) transfer to a revocable or Irrevocable trust;
 - (vi) transfer by a wholly owned Indian subsidiary company to Its holding company or vice versa;
 - (vii) transfer In the scheme of amalgamation of two Indian companies u/s 47(vl);
 - (viii) transfer in the scheme of amalgamation between two foreign companies;
 - (ix) transfer of capital asset by a banking company to a banking Institution In. the scheme of amalgamation;
 - (x) transfer in the case of business reorganization by a predecessor cooperative bank to the successor cooperative bank
 - (xi) on the conversion of a self acquired property of a member of an HUF to the joint property of the HUF.
- b) **Cost of Shares of Amalgamated Company u/s 49(2):** the cost of acquisition of shares in the amalgamating company.
- c) **Cost of acquisition in case of shares/debentures acquired on conversion of debentures u/s 49(2A):** the cost of the shares/debentures issued on conversion shall be deemed to be that part of the cost of debenture/debenture stock/deposit certificate, in relation to which such an asset is acquired by the assessee.
- d) **Cost of acquisition of shares, debentures or warrants u/s 49(2AA):** the fair market value on the date of exercise of such option.
- e) **Cost of acquisition of specified security or sweat equity shares u/s 49(2AB) read with Sec.115 WC (I)(ba):** (w.e.f. A.Y.2010-11) the fair market value of securities on the date on which the option vests with the employee. The holding period shall be reckoned from the date of allotment or transfer of such shares.
- f) **Cost of acquisition of resulting company's shares on demerger. [Section 49(2C)]**
- $$\frac{\text{Cost of acquisition of Demerged Co's Shares} \times \text{Net Book Value of assets transferred to Resulting Co.}}{\text{Net Worth of the Demerged Company before demerger}}$$
- Net Worth of demerged company = Paid up Share Capital and General Reserve as per books before demerger.
- g) **Cost of acquisition of demerged company's shares after demerger. [Section 49(2D)]**
- Original Cost of Acquisition of shares in demerged company Less Cost of acquisition of Resulting Company's shares (as calculated above)
- i) **Cost of acquisition to Transferee Company where section 47A is applicable: [section 49(3)]** - the cost of acquisition of the capital asset to the transferee company shall be the cost for which such asset was acquired by it.
- h) **Business reorganization of Co-operative Bank [Sec 49(2E)]:**
- Sec 49(2C) and Sec 49(2D) are applicable to business reorganization of a Co-operative Bank u/s 44DB.
- j) **Cost of acquisition of Bonus Shares u/s 55(2)(iiia)**
- Where bonus shares are issued prior to 1.4.81, the cost of acquisition shall be the fair market value as on 1.4.81.
 - Where such bonus shares are issued on or after 1.4.81, the cost of acquisition shall be taken as NIL.
- k) **Cost of acquisition of Original Shares u/s 55(2)(b)**
- Where the original shares were acquired prior to 1.4.81, the cost of acquisition shall be the higher of the fair market value as on 1.4.81 or the original cost of acquisition.
 - Where such shares were acquired on or after 1.4.81, the original cost of acquisition shall be considered.

l) Cost of Right Shares u/s 55(2) (aa) read with sec. 55 (2) (b)

- Cost of acquisition shall be the amount actually paid by the assessee to acquire such shares [sec.55(2)(aa)(III)]
- If such shares were acquired prior to 1.4.81, the assessee shall be entitled to opt for fair market value on 1/4/81 as the cost of acquisition.
- If the rights entitlement is renounced, the cost of acquisition of renouncing the rights entitlement to the renouncer is nil.
- Where the renounce acquires the right entitlement, the cost of acquisition of right shares to the renounce is the aggregate of (i) the amount paid to the renouncer (ii) the amount paid by him to the company/institution for acquiring such right shares [sec.55(2)(aa)(iv)].

m) Cost of acquisition of (i) shares allotted to a shareholder under a scheme of Demutualization or Corporatisation and (ii) Trading or Clearing Rights of a Recognized Stock Exchange [Sec. 55 (2) (ab)]

- The cost of acquisition Is the cost of acquisition of his original membership of the stock exchange.
- Cost of Right is taken as NIL.

14. Capital gain in case of amount received from an insurer on account of damage or destruction of any capital asset u/ s 45(1A)

Damage or destruction of assets as a result of	Chargeability
1. Flood, typhoon, hurricane, cyclone, earthquake or other convulsion of nature or	1. Chargeable as income of the year in which the money or other asset was received from the insurer.
2. Riot or civil disturbance	2. In case of receipt of other Assets the Fair Market Value (FMV) of the consideration the Asset is received.
3. Accidental fire or explosion	3. Capital Gain = Money received or FMV of Asset received Less Cost of Acquisition or indexed cost of Acquisition.
4. Action by an enemy or action taken in combating an enemy (whether with or without a declaration of war)	

Note for Depreciable Assets :

1. The **compensation received** shall be **reduced from the WDV** of the block and any **surplus** shall be chargeable as **Short Term Capital Gains** and loss shall be treated as **Short Term Capital Loss**.
2. If some **asset still exists** in the block and **no surplus is available**, then **depreciation** may be **claimed on the balance**.

Illustration 1. Ria owns a house property which was purchased by her on 1.5.1979 for ₹3 lacs. The said property was destroyed by fire on 3.4.11 and she received a sum of ₹25 lacs from the insurance company during the year. The market value of the above property as on 1.4.81 was ₹ 4,50,000. Compute capital gains for the P.Y. 2011-12.

Solution :

Computation of Capital Gains

A. Y : 2012-13

Consideration for Transfer	25,00,000
Less : Indexed Cost of Acquisition	
$4,50,000 \times \frac{785}{100}$	(35,32,500)
Long Term Capital Loss	10,32,500

Illustration 2. The w.d.v. of the block of assets as on 1.4.2011 was ₹5 lacs. Rate of Depreciation @ 15%. An asset of the same block was acquired on 11.5.11 for ₹3 lacs. There was a fire on 18.9.2011 and the assets were destroyed by fire and the assessee received a sum of ₹ 12 lacs from the insurance company. Compute the capital gain assuming:

- All the assets were destroyed by fire
- Part of the block was destroyed by fire

Would your answer differ if the assessee received ₹ 7,00,000 from insurance company assuming:

- All the assets were destroyed by fire
- Part of the block was destroyed by fire

Solution :

If Compensation received ₹ 12,00,000

Block of Assets u/s 2(11)

	Particulars	All assets sold	Part of Block sold
1.4.11	W.D.V. of the Block	5,00,000	5,00,000
	Add : Cost of New Asset purchased relating to the Block	3,00,000	3,00,000
		8,00,000	8,00,000
	(-) Compensation received	12,00,000	12,00,000
	Short Term Capital Gains	4,00,000	4,00,000
		u/s 50(2)	u/s 50(1)

If Compensation Received ₹ 7,00,000

Block of Assets u/s 2(11)

	Particulars	All assets sold	Part of Block sold	
1.4.11	W.D.V. of the Block	5,00,000	5,00,000	
	Add : Cost of New Asset purchased relating to the Block	3,00,000	3,00,000	
		8,00,000	8,00,000	
	Less : Compensation received	7,00,000	7,00,000	
	Short Term Capital Loss	1,00,000	1,00,000	= WDV
		u/s 50(2)		(Depreciation
	Less : Depreciation @ 15%		15,000	to be charged
			85,000	on WDV)

15. Capital gain on conversion of capital asset into stock-in-trade u/s 45(2)

- When a capital asset is converted into stock-in-trade, it is a transfer u/s 2(47).
- Transfer shall deemed to have taken place in the year in which the asset is so converted.
- Capital gain will arise in the previous year in which such converted asset is sold or otherwise transferred.
- Indexation of cost of acquisition and cost of improvement, if required, will be applicable for the previous year in which such conversion took place.
- Full value of consideration** = Fair Market Value of the capital asset (on the date of conversion)
- There will also arise Business Income in the previous year in which such converted asset is being sold.
- Business income** = Sale price- Fair market value of the asset on the date of conversion.

Illustration 3. Mr.B invested ₹ 2,00,000 on the purchase of gold ornaments on 10.1.90. He holds the gold ornaments as investments. On 16.1.2008. he started a business in dealing in jewellery and converts his holding into his stock-in-trade. The market value of the gold ornaments as on the date of conversion was ₹ 10,00,000 and therefore, B credited his capital account by ₹ 10,00,000 and debited stock account by ₹ 10,00,000. The gold ornaments are now reflected in the business of Mr. B. these gold ornaments were sold in the previous year 2011-12 for a sum of ₹ 15,00,000. Compute the capital gain and business income.

Solution :

The conversion of capital asset into stock-in-trade is treated as a transfer as per sec. 2(47).

Capital Asset was converted into stock-in-trade on 16.1.08 i.e. during the previous year 2007-08. Therefore, it will be treated as transfer of the previous year 2007-08. The taxability for capital gains shall arise only in the previous year in which the asset is sold i.e. previous year 2011-12.

Capital Gains for the Assessment year 2012-13

Consideration for Transfer (Market value as on the date of conversion)	10,00,000
Less : Indexed Cost of Acquisition $2,00,000 \times \frac{551}{172}$	6,40,698
Long term Capital Gains	3,59,302

Business Income for the A.Y. 2012-13

Sale Price	15,00,000
Less : Fair Market Value as on the date of conversion	10,00,000
	5,00,000

Illustration 4. Romit acquired a plot of land on 1.6.75 for ₹4,00,000. He converts the plot into stock in trade of his real estate dealing business on 18.2.2007 when the fair market value of the plot was ₹ 35,00,000. The stock-in-trade is sold by him on 18.5.2011 for ₹ 40,00,000 (FMV as on 1.4.81 was ₹ 6,00,000 and FMV as on 1.4.76 ₹4,50,00).

Solution :

The conversion of capital asset into stock-in-trade is treated as a transfer as per sec. 2(47). Capital asset was converted into stock-in-trade on 18.2.2007 i.e. previous year 2006-07.

Computation of Capital Gains

	₹
Consideration for Transfer (FMV)	35,00,000
Less : Indexed Cost of Acquisition $6,00,000 \times \frac{519}{100}$	31,14,000
Long term Capital Gains	3,86,000

Computation of Business Income

Sale Proceeds of HP	40,00,000
Less : FMV on the date of conversion	35,00,000
	5,00,000

16. Chargeability of Capital Gain on Transfer of Beneficial interest in Securities by the Depository u/s 45(2A)

Section 45(2A) was inserted by the Depositories Act, 1996. the said Act provides that dematerialisation of securities to avoid physical movement of scrips in order to ensure faster settlement of trade. In the register of the issuing company, the depository (a company registered with SEBI) appears to be a registered owner of the dematerialised securities. In the books of the depository, the real owner of the securities appears as the beneficial owner.



A depository interacts with the investors through participants (agents of depository). For this purpose investors have to enter into an agreement and open an account (which is just like a bank account) with the participant. An investor may hold his dematerialised holdings in more than one account with one or more depositories. All the transactions of sale and purchase of dematerialised securities are through the participants and are entered in the respective accounts. The ownership is transferred through book entries in the statement of accounts.

- Capital Gain accrues to the Beneficial Owner (i.e. the Investor)-taxable as the income of the beneficial owner of the previous year in which the transfer took place.
- Cost of Acquisition and period of holding is to be determined on FIFO method

Illustration 5: The depository account shows the following details of M's holdings:

Date of Credit	Particulars	Quantity
10.11.2001	Shares of XYZ LTD. purchased in physical form on 10.11.2001 @ ₹ 20 per share	300
30.11.2002	Purchased dematerialised shares of Y Ltd. on 25.11.2002 @ ₹ 70 per share	500
06.12.2004	Shares of XYZ LTD. held in physical form, were got dematerialised on 01.12.2004	

M sold 600 dematerialised shares on 6th June 2011 @ ₹ 200 per share. Brokerage is paid @2% of sale price. Compute capital gains.

Solution :

- Person Liable : The sale of shares held under Dematerialized format with a depository is chargeable to tax as the income of the beneficial owner.
- Cost of Acquisition and period of holdings : The cost of acquisition and the period of holding shall be determined on FIFO Method. [Circular No. 768 datd 24.6.1998]
 - FIFO method will be applied for each account independently.
 - When physical stock is dematerialized, the date of credit into the depository account shall be considered for the purpose of FIFO method, but indexed cost of acquisition shall be computed on the basis of year of acquisition.

	₹
Consideration for Transfer	
600 Share @ ₹ 180 per share	1,20,000
Less : Indexed Cost of Acquisition	(61,465)
(i) $500 \times 70 \times \frac{785}{447}$	
(ii) $100 \times 20 \times \frac{785}{480}$	(3,271)
Long Term Capital Gain	55,264

17. Capital gain on transfer of capital asset by a partner/member to a firm/AOP/BOI as capital contribution u/s 45(3)

- There shall arise capital gain from the transfer of capital asset held by a person, to a firm or AOP or BOI in which he is or becomes a partner or member. . Such transfer of capital asset may be by way of capital contribution or otherwise.
- It shall be chargeable to tax as his income of the previous year in which such transfer took place.
- **Full value of consideration** (for computing capital gains) = the amount recorded in the books of accounts of the firm.

- **Market value of the asset on the date of transfer is not relevant.**
- Cost of acquisition and cost of improvement shall be allowed to be indexed accordingly.

Illustration 6. Nisith acquired a property by way of gift from his father in the previous year 1988-89 when its FMV was ₹3 lacs. His father had acquired the property during 1981-82 for ₹ 4 lacs. This property was introduced as capital contribution to a partnership firm in which Nisith became a partner on 15.6.2011. The market value of the asset as on that date was ₹ 20 lacs, but it was recorded in the books of account of the firm at ₹ 17 lacs. Is there any capital gain chargeable in the hands of Mr. Nisith?

Solution :

Computation of Capital Gains		A.Y : 2012-13
		₹
Consideration for Transfer		17,00,000
Less : Indexed Cost of Acquisition		
	$4,00,000 \times \frac{785}{161}$	19,50,311
Long Term Capital Loss		2,50,311

- Full value of consideration is taken as the value at which it is recorded in the books of accounts of the firm.
- Cost of acquisition is taken as cost to the previous owner but indexation has been done from the date it was first held by the assessee.
- Market value of the asset on the date of transfer is not relevant.

Illustration 7. Ayan has two motor cars which are used by him exclusively for his personal purposes. The cost of the cars was ₹ 6,50,000 and ₹ 8,00,000. The first car was transferred by him on 15.1.2012 to a firm in which he is a partner as his capital contribution. The market value of the car as on 15.1.2012 is ₹ 5,00,000, but it was recorded in the books of account of the firm at ₹ 6,00,000. Compute the capital gain if any, chargeable for the A.Y. 2012-13.

Solution :

Since the car is a moveable property and was used by Mr. Ayan for his personal purposes only, it will be treated as a personal effect.

W.e.f. A.Y. 2008-09, "Personal effect" means moveable property including wearing apparel and furniture held for personal use by the assessee or any member of his family dependent on him but excludes :

- Jewellery
- Archaeological collections
- Drawings
- Paintings
- Sculptures
- Any work of art.

18. Capital gain on transfer of a capital asset by way of distribution on the dissolution of a firm, AOP, BOI u/s 45(4)

- **Transfer:** Distribution of a Capital Asset by a Firm / AOP / BOI on its dissolution or otherwise is a transfer.
- **Year of Taxability:** Capital gain shall be chargeable to tax in the hands of Firm/ AOP/BOI in the previous year in which such transfer takes place.
- **Capital gain** = Fair Market Value on the date of transfer Less Cost or Indexed cost of acquisition.
- **Depreciable Assets:** Transfer of depreciable asset results in short-term capital gain or loss u/s 50.

Illustration 8. PQR & Co. is a partnership firm, consisting 3 partners P, Q and R. the firm is dissolved on 31.12.11. The assets of the firm were distributed to the partners as under :

Particulars	Block of machinery (given to P)	Stock (given to Q)	Land (given to R)
Year of acquisition	1990-91	2002-03	1978-79
Cost of acquisition (₹)	7,20,000	4,00,000	10,000
Market value as on 31.12.11	15,00,000	6,00,000	25,00,000
WDV as on 31.12.11	10,40,000	—	—
Value at which given to partners as per agreement	10,00,000	4,50,000	18,00,000
Market value as on 1.4.81	—	—	2,70,000

Compute the income taxable in the hands of the firm for the assessment year 2012-13. What shall be the cost of acquisition of such assets to the partners of the firm?

Solution :

Computation of Short Term Capital Gains on block of machinery

	₹
Sale consideration (i.e. the market value)	15,00,000
Less : Cost of Acquisition (WDV of the block)	10,40,000
Short Term Capital Gains	4,60,000

Income from Business (on transfer of stock)

	₹
Market value of stock	6,00,000
Less : Cost of Acquisition	4,00,000
	2,00,000

Computation of Capital Gains on transfer of land

	₹
Consideration for transfer	25,00,000
Less : Indexed cost of Acquisition : $2,70,000 \times \frac{785}{100}$	21,19,500
	3,80,500

Cost of acquisition of assets to the partners

	₹
Partner "P"	1,00,000
Partner "Q"	4,50,000
Partner "R"	18,00,000
Less : Indexed cost of Acquisition : $2,70,000 \times \frac{785}{100}$	21,19,500
	2,30,500

Illustration 9. A firm consists of 3 partners X, Y & Z. Z retires from the firm on 15.10.2011. His capital balance and the profits till the date of retirement stood at ₹ 16 lacs. The firm transferred Its land to Z in settlement of his account. The market value of the land as on that date was ₹ 30 lacs. The land was acquired by the firm on 1.5.93 for ₹ 4 lacs.

Compute the capital gains in the hands of the firm.

Solution :

Computation of Long Term Capital Gains for the A.Y. 2012-13

	₹
Consideration for Transfer	30,00,000
Less : Indexed Cost of Acquisition	12,86,885
$4,00,000 \times \frac{785}{244}$	
Long Term Capital Gain	17,13,115

19. Capital gain on transfer by way of compulsory acquisition of an asset u/s 45(5)

- **Chargeability:** It is a transfer u/s 2(47) chargeable to tax under the head **Capital Gains**.
- **Taxability of Normal/Original Compensation [Section 45(5)(a)]**
 - Normal or **original compensation** Is taxable in the previous year in which it is first received.
 - **Whole of the compensation is taxable** even if a portion of the amount is received.
 - Capital Gain = Whole of the normal compensation Less Cost or Indexed cost of Acquisition.
- **Indexation** shall be applied for the year in which the asset is compulsorily acquired.
- **Taxability of Enhanced Compensation [Section 45(5)(b)]**
 - **Enhanced compensation** shall be taxable in the previous year in which it is received.
 - The Cost of acquisition and the cost of improvement shall be taken as 'NIL'.
 - Capital Gain = Enhanced Compensation received Less Expenses on Receipt of Enhanced Compensation
- **Compensation received by Legal Heirs:** The **Compensation** received subsequent to the **death of the assessee is taxable** in the hands of his legal heirs.
- **Reduction of Compensation:** Where normal compensation / enhanced compensation is reduced by Court or Tribunal, then the **Capital Gain shall be recomputed** accordingly.
- **Interest on enhanced compensation** on account of compulsory acquisition is chargeable under the head "Income from other sources".

Illustration 10. Mr. B acquired a house property for ₹ 50,000 in 1969-70. On his death in October 1985 the house was acquired by his son C. The market value of the house as on 1/4/81 was ₹ 3,00,000. This house was acquired by the Government on 15.3.2008 and a compensation of ₹ 16 lacs is paid to him on 25.3.2011. C filed a suit against the Government challenging the quantum of compensation and the court ordered for giving additional compensation of ₹ 14,00,000. He incurred an expenditure of ₹ 40,000 as an expenditure in connection with the suit. The additional compensation was received on 25.3.2012. Compute capital gains chargeable to tax.

Solution :

Capital Gain on initial compensation shall be chargeable in the A.Y. 2011-12, i.e. for the previous year 2010-11.

Computation of Long Term Capital Gains for the A.Y. 2011-12

	₹
Consideration for transfer (being the compensation)	16,00,000
Less : Indexed Cost of Acquisition $3,00,000 \times \frac{711}{133}$	16,03,759
Long Term Capital Loss	3,759

Note : This loss shall be carried forward for adjustment only against Long Term Capital Gains arising within the next 4 assessment years.

Computation of Long Term Capital Gains for the A.Y. 2012-13

	₹
Enhanced Compensation received	14,00,000
Less : Cost of Acquisition	NIL
Cost of Improvement	NIL
Expenses on Transfer	(40,000)
Long Term Capital Gains	13,60,000
Less : Long Term Capital loss – Set off from the A.Y. 2011-12	(3,759)
Balance of LTCG	13,56,241

20. Capital gain on conversion of debentures into shares

- Conversion of debentures into shares is exempted u/s 47(x)
- In case of subsequent transfer by the transferee, the holding period in the hands of the transferee u/s 2(42A) shall not include the holding period of the earlier asset.
- Cost of new asset in the hands of the transferee u/s 49 shall be the cost at which old asset is converted.

Illustration 11. R acquired 400 listed debentures of ₹100 each on 15.9.2010. 50% value of the debentures was converted into 4 listed equity shares of the face value of ₹10 each on 20.8.2011. R therefore, received 800 shares of face value of ₹10 each and left with 200 debentures. The shares were sold on 25.12.11 @ ₹100 per share through recognized stock exchange and R paid ₹200 as securities transaction tax. Compute the capital gains chargeable for the assessment year 2012-13.

Solution :

Conversion of Debentures into shares is exempted from Transfer u/s 2(47)(x).

Now these shares are sold within a period of 12 months. It is a Short-term Capital asset.

Computation of Long-Term Capital Gains for the A.Y. 2012-13

	₹
Consideration for transfer of 800 shares @ ₹100 each	80,000
Less : Cost of Acquisition (200 × 100)	20,000
Short Term Capital Gains	60,000

21. Capital gains on distribution of assets by companies in liquidation u/s 46

No capital gain to company on distribution of assets to shareholders on liquidation u/s 46(1) provided the distribution of assets in specie (i.e. in the same form).

22. Shareholders liable to capital gain tax on receiving money and asset on the liquidation of the company:

Where a shareholder on the liquidation of a company, receives any money or other asset from the company in lieu of the shares held by him, such a shareholder shall be chargeable to income tax under the head Capital gains in respect of the excess money and the assets so received over the cost of the shares held by him.

In this case, the consideration price for capital gain purposes shall be money received and/or the market value of the other assets on the date of distribution minus deemed dividend within the meaning of Sec.2(22)(c).

Any distribution made to the shareholders of a company on its liquidation, to the extent to which the distribution is attributable to the accumulated profits of the company immediately before its liquidation, whether capitalized or not.

Accumulated profits for a company in liquidation includes all profits of the company upto the date of liquidation. Accumulated profits should include the credit balance of profit and loss account, general reserves, investment allowance, capitalized profits and profits of the year upto the date of distribution/liquidation.

However, provisions and reserves meant for specific liability, to the extent of the liability shall not be included. Provision for income tax, provision for dividend, reserve for depreciation do not form part of the accumulated profits.

- Securities premium is not accumulated profits.
- It may consist of exempted incomes, like agricultural income.
- It will include current profits and all profits of the company till the date of liquidation, subject to the exception provided therein.

Illustration 12. A holds 15,000 shares (10% of total share holding) in B Ltd. which he had purchased on 10.2.96 for ₹ 6,00,000. The company went into liquidation on 16.7.2011 and paid a sum of ₹ 20 per share in cash and an asset whose market value as on the date of distribution i.e. 5.10.11 was ₹ 18,20,000 to A. the accumulated profits of the company were ₹ 15 lacs.

(a) Compute the income of A for the A.Y. 2012-13 assuming that he has no other income.

(b) Compute the capital gain chargeable to tax if the asset of B Ltd. is sold by A for ₹ 15 lacs on 28.3.12.

Solution :

Computation of Capital Gains of Mr. B for the A.Y. 2012-13

	₹
(a) (i) Capital Gain on transfer of shares	
Total consideration (15,000×20+18,20,000)	21,20,000
Less : Proportionate amount of deeme dividend (10% of ₹ 12,86,353)	1,28,635
Less : Indexed Cost of Acquisition $6,00,000 \times \frac{785}{281}$	16,76,157
Long Term Capital Gains	4,43,843
(ii) Income from others Sources	
Dividend from Indian Company	Exempted
	4,43,843
(b) Capital Gain on transfer of asset (B Ltd.)	
Full Value of Consideration	15,00,000
Less : Cost of Acquisition (being the market value as on the date of distributions)	13,20,000
Short Term Capital Gains	1,80,000
Accumulated Profits	15,00,000

Dividend tax @ 16.60875% (= 15% + 7.5% + 2% Education cess + 1% SHEC)

Hence, the amount to be distributed plus tax @ 16.60875%

on such amount should be ₹ 15,00,000

$$\therefore \text{Amount of tax} = 15,00,000 \times \frac{16.60875}{116.60875} = ₹ 2,13,647$$

$$\therefore \text{Profits available for distribution} = ₹ (15,00,000 - 2,13,647) = ₹ 12,86,353.$$

23. Capital gain on sale of goodwill of a business, trademark or brand name, tenancy rights, route permits or loom hours, right to manufacture or right to carry on any business.

The following are chargeable to tax as capital gains:

- Goodwill of a business. There will not arise any capital gain on the goodwill of a profession.
- Trademark or brand name associated with the business;

- (iii) Right to manufacture, produce or process any article or thing, for a consideration e.g. patent, copyright, formula, design.
- (iv) Right to carry on any business;
- (v) Tenancy rights;
- (vi) Route permits;
- (vii) Loom hours.

Cost of acquisition u/s 55(2) (a)

- (a) If the assets are purchased- original cost of acquisition.
- (b) In any other case- nil

Cost of improvement

- (a) In case of goodwill of a business, right to manufacture, produce or process any article or thing and right to carry on any business (whether self generated or purchased), shall always be taken as nil.
- (b) For the other assets as mentioned above, it shall be taken as the actual capital expenditure incurred by the assessee on the improvement of that asset, whether such asset is self generated or purchased.

Computation of Capital Gains in case of Self Generated Goodwill of a Business (Not of a profession), Right to Manufacture/Produce/Process an article or right to carry on any business.

Particulars	₹	₹
Sale Consideration (Actual Amount)		xxx
Less: Expenses of Transfer Actual Amount		xxx
Net Consideration		xxx
Less: Cost of Acquisition	NIL	
Less: Cost of Improvement	NIL	NI
Taxable Capital Gains		xxx

Computation of Capital Gains in case of Self Generated Tenancy Rights, Route Permits, Loom Hours, Trade Marks, Brand Name related with business —

Particulars		₹
Sale Consideration (Actual Amount)		xxx
Less: Expenses of Transfer (Actual Amount)		xxx
Net Consideration		xxx
Less: Cost of Acquisition	NIL	
Less: Cost of Improvement (Actual Amount)	XXX	xxx
Taxable Capital Gains		xxx

Illustration 13. (a) P commenced a business on 10.5.92. The said business is sold by P on 25.8.11 and he received ₹ 10 lacs towards goodwill.

(b) What will be your answer in the above case, if P had acquired the goodwill for this business for a consideration of ₹ 3,00,000.

Solution :

Computation of Long Term Capital Gains for the A.Y. 2012-13

	₹
(a) Consideration for transfer	10,00,000
Less : Indexed Cost of Acquisition (Self-Generated)	NIL
Long term Capital Gains	10,00,000
(b) Consideration for transfer	10,00,000
Less : Indexed Cost of Acquisition = $3,00,000 \times \frac{785}{223}$	10,56,054
Long term Capital Loss	56,054

Illustration 14. R has been living in a rented accommodation since August 1983, and he is paying a rent of ₹ 4000 per month. The landlord got the house vacated from R on 16.7.2011 and paid a sum of ₹ 5 lacs for vacating the house.

Compute Capital Gains, if any, in the hands of R.

Solution :

Computation of Long Term Capital Gains for the A.Y. 2012-13

	₹
Consideration for transfer	15,00,000
Less : Indexed Cost of Acquisition (Self-Generated asset)	NIL
Long term Capital Gains	15,00,000

Illustration 15. Mr. Nitin is a Chartered Accountant practicing in Delhi since January 1983. He transfers the practice to another Chartered Accountant on 15.7.2011 and charges ₹ 10 lacs for goodwill.

Solution :

Since the asset transferred is Goodwill of a profession and not of a business, it is treated as self-generated asset and there is no capital gain on self-generated asset.

Illustration 16. R purchased tenancy right on 1.4.1980 for ₹ 4,60,000. The same was sold by him on 14.8.2011 for ₹ 45 lacs. FMV of tenancy right as on 1.4.81 ₹ 6,50,000.

Solution :

Computation of Long term Capital Gains for the A.Y. 2012-13

	₹
Consideration for transfer	45,00,000
Less : Indexed Cost of Acquisition $4,60,000 \times \frac{785}{100}$	36,11,600
Long term Capital Gains	8,89,000

Illustration 17. R purchased 1200 shares on 1.4.80 for ₹ 40 each. He was allotted 1200 right shares on 1.5.80 for ₹ 50 each. He was also allotted 2,400 bonus shares on 1.3.81. Again, on 4.5.91, he was further allotted 4,800 right shares for ₹ 80 each. Further on 27.9.01, he was allotted 4,800 bonus shares. The fair market value of these shares on 1.4.81 was ₹60 each. All the above shares are sold by R on 16.10.11 for ₹ 400 per share. Compute the capital gains assuming :

- The above shares are not sold through recognized stock exchange.
- The above share is sold through recognized stock exchange and necessary securities transaction tax was paid by R.

Solution :

- (a) Where Shares were not sold through recognised stock exchange

Computation of Capital Gains for the A.Y. 2012-13

	₹
Capital Gain on original shares purchased on 1.4.80	57,60,000
Consideration for transfer (14,400×400)	
Less : Indexed Cost of Acquisition	
(i) $1,200 \times 60 \times \frac{785}{100}$	5,62,200
(ii) $1,200 \times 60 \times \frac{785}{100}$	5,65,200
(iii) $2,400 \times 60 \times \frac{785}{100}$	11,30,400
(Bonus shares issued prior to 1.4.81 shall opt for Fair market value as on 1.4.81 and shall be allowed to be indexed)	
(iv) $4,800 \times 80 \times \frac{785}{199}$	15,14,774
(v) Cost of Acquisition for Bonus shares after 1.4.81	NIL
	19,84,426

- (b) Where shares are sold through recognised stock exchange and securities transaction tax has been paid by the assessee, entire long term capital gain on there share shall be exempted u/s 10(38)

24. CAPITAL GAINS U/S 50B in case of SLUMP SALE U/S 2(42C)

Slump Sale means the transfer of one or more undertakings as a result of the sale for a lump sum consideration without values being assigned to the individual assets and liabilities in such sales.

Cost of acquisition and cost of improvement in case of slump sale: "Net Worth" of the undertaking or the division. (NO INDEXATION OF SUCH COSTS WILL BE ALLOWED).

Note : Cost of acquisition of assets in case of slump sale of business specified under section 35AD [Section 50B] [W.e.f. A.Y. 2010-11]

Section 50B relating to slump sale amended: While computing the net worth in case of slump sale for the purpose of computing capital gain, in the case of capital assets in respect of which the whole of the expenditure has been allowed or is allowable as a deduction under section 35AD, its cost shall be taken as NIL.

NET WORTH = AGGREGATE VALUE OF TOTAL ASSETS of the undertaking or division as reduced by the VALUE OF LIABILITIES of such undertaking or division as appearing in its books of account.

Aggregate value of total assets:

- In case of depreciable assets- the written down value of the block of assets.
- In case of any other assets- the book value of such assets.

Note :

- Any change in the value of assets on account of revaluation of assets shall be ignored for the purposes of computing the net worth.
- Benefit of unabsorbed losses and unabsorbed depreciation of the undertaking transferred shall not be available to the transferee company.
- If the business is transferred on "severable sale" basis, the surplus will be short-term capital gains in case of depreciable assets. While in case of other assets, it may be short- term or long-term depending upon the holding period.

- (4) No profit under the head profit or gains from business or profession shall arise even if the stock of the said undertaking is transferred alongwith other assets.
- (5) Determination of value for stamp duty, registration fees shall not be regarded as assigning values to individual assets or liabilities.
- (6) Report of a Chartered Accountant in prescribed Form 3CEA shall be enclosed.

Illustration 18. X Ltd. has two divisions namely A and B the Balance Sheet as at 31.3.2012.

			A	B	Total
Paid up capital	6,00,000	Fixed Assets (W.D.V. as on 31.3.12)		6,00,000	6,00,000
		Land & Building		1,50,000	1,50,000
		Plant & Machinery		2,50,000	2,50,000
		Investments	—	2,00,000	2,00,000
		Debtors	2,00,000	3,00,000	5,00,000
		Stock-in-trade	1,50,000	4,00,000	5,50,000
		Other current assets			
Reserves & Surplus	8,40,000		50,000	40,000	90,000
Creditors :	3,00,000				
Paints Division	6,00,000				
Tyre Division	23,40,000				23,40,000

The company decides to sell the paint division which was established in 1983 to another company G Ltd. on 1.5.2011 for a lump sum of ₹ 14 lacs. The fixed assets of the company includes land and building whose W.D.V. as on 1.4.08 is ₹ 15 lacs, but it has been valued as ₹ 5 lacs for the purpose of stamp duty. Compute the capital gain taxable in the aforesaid case assuming that the market value of the stock transferred is ₹ 2 lacs.

Solution :

Computation of Capital Gains for the A.Y. 2012-13

		₹
Consideration for transfer		14,00,000
Less : Net worth of the division		
Land and Building (WDV)	1,50,000	
Plant & Machinery (WDV)	2,50,000	
Debtors (Book Value)	2,00,000	
Stock (Book Value)	50,000	
Others Current Assets (Book Value)	<u>40,000</u>	
	7,90,000	
Less : Liabilities	<u>3,00,000</u>	4,90,000
Long term Capital Gains		9,10,000

25. Capital gain on re-purchase of Units of Mutual Funds under Equity Linked Savings Scheme u/s 45(6)

1. Where a shareholder receives any consideration from the company for purchase of Its own shares or other specified securities, it is a **transfer chargeable under the head Capital Gains**.
2. The capital gain is **chargeable to tax in the previous year** in which the shares or securities are purchased by the Company.



3. **Capital Gains** = Value of Consideration Received **Less** Cost of Acquisition or Indexed cost of acquisition.
4. In case of buy back of shares, there is no question of deemed dividend u/s 2(22) (d).

26. Capital gains on purchase by company of its own shares or other specified securities u/s 46A

Capital gain = (Value of consideration received by the shareholder) - (cost of acquisition of such specified securities)

Specified securities has been defined as per Sec.77A of the Companies Act,1956.

Specified securities includes employees stock option or other securities as may be notified by the Central Government from time to time.

27. Capital Gains on violation of the provision of Sec. 47(iv) and 47(v) due to withdrawal of exemption u/s 47A.

Illustration 19. R Ltd. is a wholly owned subsidiary company of S Ltd. Both R Ltd. and S Ltd. are Indian companies. R Ltd. transferred a plot of land to S Ltd. on 21.10.1982 for ₹ 3 lacs. R Ltd. had acquired this land on 1/1/76 for ₹ 80,000. The market value as on 1.4.81 was ₹ 1,50,000. What would be the capital gains if any, chargeable in the hands of R Ltd and S Ltd. in the following situations:

- (a) S Ltd. sells the land on 2.9.11 for ₹ 12 lacs. S Ltd. continues to hold 100% shares of R Ltd.
- (b) S Ltd. converted the land as its stock-in-trade on 5.10.88 and then sold it on 12.9.11 for ₹ 16 lacs. The market value of the asset on 5.10.88 was ₹ 8 lacs.

Solution :

S. Ltd.

Computation of Capital Gains for the A.Y. 2012-13

	₹
(a) (i) Consideration for Transfer	12,00,000
Less : Indexed Cost of Acquisition	10,80,275
$1,50,000 \times \frac{785}{109}$	
Long Term Capital Gains	1,19,725

- (ii) There will be no capital gains for R Ltd. neither in the year of transfer to S Ltd. nor in the year by S Ltd, as the land has not been converted into stock and it remains a wholly owned subsidiary company.

(b) (i) In the case of R Ltd.

Since the land has been converted into stock-in-trade on 05.10.88 which falls within eight years of the original transfer, there will be capital gains to R Ltd. and its assessment for the A. Y. 83-84 (P. Y: 82-83) will be rectified u/s 155 as under :

Consideration for transfer (amount at which it is transferred to S Ltd.)	3,00,000
Less : Cost of Acquisition	<u>80,000</u>
Long term Capital Gains	<u>2,20,000</u>

The LTCG of ₹ 2,20,000 will be included in the total income for the A.Y. : 83-84 and taxed according to the provisions applicable at that time.

- (ii) Although the land was converted into stock-in-trade on 5.10.08, it will be regarded as transfer, but capital gain on such transfer will be taxable in the previous year in which such converted on it is sold. The cost of acquisition in this case will be the value at which the asset was transferred to it.

Computation of Capital Gain for the A.Y. 2012-13

	₹
Consideration for transfer (being the Market value as on the date of conversion)	8,00,000
Less : Indexed Cost of Acquisition $3,00,000 \times \frac{161}{100}$	4,83,000
Long term Capital Gains	3,17,000

28. EXEMPTIONS OF CAPITAL GAINS

1. Capital gain on transfer of units of US 64 exempt if transfer takes place on or after 1.4.02 u/s **10(33)** w.r.e.f. A.Y. 2005-06.
2. Long-term capital gain on eligible equity shares exempt If the shares are acquired within a certain period u/s **10(36)** w.e.f. A.Y. 2006-07. these assets must have been acquired on or after 1.3.03 but before 1.3.04 and held for a period of more than 12 months.
3. Exemption of capital gains on compensation received on compulsory acquisition of agricultural land situated within specified urban limits u/s **10(37)** w.r.e.f. A.Y. 1.4.05.
 - (a) Where the compulsory acquisition has taken place before 1.4.05 but the compensation is received after 31.3.05, it shall be exempt.
 - (b) If the part of the original compensation in the above case has already been received before 1.4.05, then the exemption shall not be available even though the original compensation is received after 31.3.05.
 - (c) If enhanced compensation is received on or after 1.4.05 against agricultural land compulsorily acquired before 1.4.05 shall be exempt.
4. Exemption of long term capital gain arising from sale of shares and units u/s **10(38)** w.e.f. 1.10.05. Any income arising on or after 1.10.05 from the transfer of a long-term capital asset, being an equity share in a company or a unit of an equity oriented fund shall be exempted provided:
 - (a) Such equity shares are sold through recognized stock exchange, whereas units of an equity oriented fund may either be sold through the recognized stock exchange or may be sold to the mutual fund.
 - (b) Such transaction is chargeable to securities transaction tax.
5. Exemption of capital gain on transfer of an asset of an undertaking engaged in the business of generation, etc of power u/s 10(41), provided such transfer is effected on or before 31.3.07 to the Indian company notified u/s 80 IA(v)(a).

29. Explain the tax treatment of Capital Gain on transfer of shares, debentures of Indian Company held by non-residents. [Section 48 (Proviso) read with Rule 115A].

1. Applicability: All Non-Residents Including Foreign Companies except persons covered u/s 115AC & 115AD.
2. Assets Transferred: Shares or Debentures In an Indian Company.
3. Nature of Capital Gain: Short Term or Long Term
4. Average TT Rate = (Buying Rate + Selling Rate adopted by State Bank of India)/2

Computation of Capital Gains

Particulars	Value in ₹	Conversion Rate	Value in Foreign Curr.
Sale Consideration	xxxx	Avg. TT Rate on the date of Transfer	xxx
Less: Expenses on Transfer	<u>(xxx)</u>	Avg. TT Rate on the date of Transfer	(xxx)
Net Consideration	xxxx		xxx
Less: Cost of Acquisition	<u>(xxxx)</u>	Avg. TT Rate on the date of Acquisition	(xxx)
Capital Gain in Foreign Currency			xxx
Capital Gain in ₹		Capital Gain In Foreign Currency × Buying Rate on the date of Transfer	xxx
Less: Exemption u/s 115F, wherever applicable		<u>Capital Gains × Amount invested</u> Net consideration	(xxx)
Taxable Capital Gain			xxx

Note : Indexation Benefit is not available.

30. What are the conditions and exemption from long-term capital gains on transfer of foreign exchange asset by a Non-Resident Indian [Section 115F]

- Condition :** Long-term capital gain on transfer of foreign exchange asset Is entitled for exemption If the whole or part of the net consideration is Invested within 6 months after the date of such transfer in prescribed assets.
- Prescribed Assets:**
 - Shares of an Indian Company or debentures of an Indian Public Limited Company.
 - Deposit with an Indian Public limited Company.
 - Central Government securities.
 - National Savings Certificates VI and VII issue.
- Exemption:** If the **whole of the net consideration** is invested, then entire capital gain is exempt.
If a part of the net consideration is invested, then the deduction shall be computed as follows:

$$\text{Amount Exempted} = \text{Capital Gains} \times \text{Amount Invested/Net consideration}$$
- Holding period of the asset:** 3 years from the date of acquisition.
- Sale/conversion within the holding period:** Amount exempted shall be chargeable to tax as Long Term Capital Gain In the year of transfer.

31. Explain the tax treatment of income from Deep Discount Bonds (DDBs).

- Income based on Market Value:**
 - Market Value:** Market Value of DDBs will be determined at the end of every financial year, 31st March, that is, as per the values declared by RBI or Primary Dealers Association of India, jointly with the Fixed Income Money Market and Derivatives Association of India.
 - Income:** The difference between market values on the opening and closing dates of that financial year constitutes income of that year.
 - Computation of Income:** The income chargeable will be computed as under
 - For Original Subscribers:** Difference between market values on 31st March (Closing date) and 1st April (Opening date) of that financial year.

- **For Subsequent purchasers:** Difference between market values on 31st March (Closing date) and cost of Purchase of bond.

(d) **Taxable as-** this income will be treated as interest in case of investors and business income in case of traders.

2. **Transfer before maturity:** If the bondholder transfers the bond before maturity

(a) **In case of Investors:**

Capital Gains = Sale Price **Less** Cost of Acquisition of the Bond

Nature of Capital Gain: Capital Gain is always **Short-Term** since income is offered upto 31st March of the previous year and the holding period will always be less than 12 months.

Cost of Bond = Cost of Acquisition (subscription price paid by original investor or purchase price paid by intermediate purchaser) and the income already offered to tax by the bondholder upto the date of transfer.

(b) **In case of Traders:** Business Income = Sale Price **Less** Cost of Acquisition of the Bond

3. **Redemption on Maturity:**

(a) If the **original subscriber redeems the DDB**

- **In case of Investors:**

Interest Income = Redemption Price **Less** Market Value as on the last valuation date immediately preceding the maturity date

- **In case of Traders:**

Business Income = Redemption Price **Less** Market Value as on the last valuation date immediately preceding the maturity date

(b) **If an intermediate purchaser redeems the DDB**

Interest or Business Income = Redemption Price **Less** Cost of the Bond to such purchaser **Cost** = Cost of Acquisition (subscription price paid by original investor or purchase price paid by intermediate purchaser) and the income already *offered* to tax by the bondholder upto the date of redemption.

32. Write short notes on Capital Gains on Sale of Property at less than Government Value. [Sec. 50C]

1. **Nature of Asset:** Land or Building or both

2. **Consideration for transfer:** Amount is less than the value adopted or assessed by the State Government Authority (referred to as the "Stamp Valuation Authority for the purpose of payment of stamp duty.")

3. **Value to be adopted for Capital Gains:** Value adopted by the Stamp Valuation Authority.

Provisions for deemed valuation of immovable property in certain cases of Transfer [Section 50C] [W.e.f. A.Y. 2010-11] — Further, new Explanation 2 has been inserted to section 50C(2) so as to clarify the meaning of the term 'assessable'.

'Explanation 2.—For the purposes of this section, the expression "assessable" means the price which the stamp valuation authority would have, notwithstanding anything to the contrary contained in any other law for the time being in force, adopted or assessed, if it were referred to such authority for the purposes of the payment of stamp duty'.

4. Reference to Valuation Officer:

- The assessee can claim that the value adopted or assessed by the Stamp Valuation Authority exceeds the Fair Market Value of the property as on the date of transfer.
- Value adopted by the Stamp Valuation Authority is **not disputed before any authority or Court.**
- In such case, the Assessing *Officer* may refer the case to the Valuation *Officer*.
- Where the value determined by the Valuation *Officer* **exceeds the value adopted by the Stamp Valuation Authority**, the Capital Gain shall be considered as follows—
Capital Gains = Value adopted by Stamp Valuation Authority **Less** Cost or Indexed Cost of Acquisition.



33. Advance money received on capital gains [Section 51]

1. **Reduce from Cost/WDV/FMV :** Any advance money or any other sum received and retained by the assessee is to be reduced either from
 - (a) Cost of Acquisition; or
 - (b) Written Down Value; or
 - (c) Fair Market Value.
2. **Applicability:** This provision is applicable only when the transfer as per the original agreement does not take place and the advance money is received and forfeited by the assessee as per the agreement.

Illustration 20 : Rohit purchased a house in Delhi in December 2004 for ₹ 2,50,000. In March 2011, he entered into an agreement to sell the property to Z for a consideration of ₹ 5,00,000 and received an earnest money of ₹ 50,000. As per the terms of agreement, the balance payment was to be made within 30 days of the agreement. If the intending purchaser does not make the payment within 30 days, the earnest money would be forfeited. As Z could not make the payment within the stipulated time the amount of ₹ 50,000 was forfeited by Rohit. Subsequently, on 16.6.11, Rohit sold the house to Mohit for ₹ 6,00,000. He paid 3% brokerage on sale of the house. Compute capital gains chargeable to tax for the assessment year 2012-13.

Solution :

Computation of Capital Gains for the A.Y. 2012-13

	₹
Consideration for transfer	6,00,000
Less : Expenses on transfer (Brokerage @ 3% on 6,00,000)	18,000
Net Consideration	5,82,000
Less : Indexed Cost of Acquisition	
Cost of Acquisition	2,50,000
Less : Amount received and forfeited (u/s 51 to be adjusted against cost)	<u>50,000</u>
Net Cost of Acquisition	<u>2,00,000</u>
∴ Indexed Net cost of Acquisition	
$= 2,00,000 \times \frac{785}{480}$	3,27,083
Long Term Capital Gains	2,54,917

34. Reference to Valuation Officer [Section 55A]

Under the following circumstances the Assessing Officer may refer the valuation of the capital asset to the Valuation Officer and his valuation report shall be binding on the Assessing Officer-

1. Where the value of the asset is estimated by the registered valuer but the Assessing Officer is of the opinion that the **value so determined is less than its fair market value.**
2. In any other case, the Assessing Officer is of the opinion that
 - (a) The **fair market value** of the asset **exceeds the value of the** 'assets declared by the assessee either by more than 15% or by ₹ 25,000 (Rule 11AA); or
 - (b) The nature of the asset and other relevant circumstances are such that, It is necessary to do so.

EXEMPTIONS FROM CAPITAL GAINS

35. EXEMPTIONS FROM CAPITAL, GAINS FOR TRANSFER OF RESIDENTIAL HOUSE PROPERTY u/s 54

Applicability	Individual / HUF
Asset Transferred	Residential House Property
Nature of the Asset	Long Term Capital Asset
New Asset to be acquired	Residential House Property
Amount to be Invested In New Asset	Long Term Capital Gain on Transfer
Amount of Exemption	Least of: (a) Amount invested in New Residential House, or (b) Capital Gain
Time Limit for Investment	(a) For Purchase: Within one year before or two years after the date of transfer (b) For Construction: Within three years after the date of transfer.
Unutilized Amount	(a) Amount not utilized before the due date of filing return shall be kept in Capital Gain Account Scheme of a Nationalized Bank. (b) The amount should be utilized within the prescribed period. (c) Amount not utilized within the prescribed period shall be treated as L TCG of the previous year in which prescribed period expires.
Holding Period of New Asset	Three years from the date of acquisition or construction
Sale of New Asset within holding period	Short Term Capital Gain computed as follows - Sale Consideration of New Asset Less Cost of Acquisition reduced by Capital Gains exempted u/s 54

Illustration 21: Ravi owns a residential house which was purchased by him in 1975 for ₹ 80,000. The FMV as on 1.4.81 was ₹ 2,00,000. This house is sold by him on 16.7.2011 for a consideration of ₹ 15,00,000. The brokerage and expenses on transfer was ₹ 15,000. Compute capital gains for the assessment year 2012-13.

If he invests ₹ 5,00,000 for purchase of a new house on 15.3.2012.

If the HP so purchased in 15.3.2012 is again sold in 21.10.12 for ₹ 9 lacs, what will be the tax liability?

Solution :

Computation of Capital Gains for the A.Y. 2012-13

	₹
Consideration for transfer	15,00,000
Less : Expenses on transfer	15,000
Net Consideration	14,85,000
Less : Indexed Cost of Acquisition $2,00,000 \times \frac{785}{100}$	15,70,000
Long term Capital Loss	85,000
Less : Exemption u/s 54	
Cost of New HP Purchased ₹ 5,00,000 (exemption restricted upto the balance of LTCG)	NIL
Taxable Long term Capital Loss	85,000

If the HP purchased in 15.3.2012 is again sold on 21.10.12 for ₹ 9 lacs, there share a rise short term capital gains. The cost of acquisition shall be adjusted to the extent of long term capital gains exemption already availed.

Computation of Capital Gains for the A.Y. 2013-14

	₹
Consideration for transfer	9,00,000
Less : Cost of Acquisition	
Cost of purchase	5,00,000
Less : Exemption u/s 54 availed during A.Y. 2012-13	<u>NIL</u>
now withdrawn	5,00,000
Short term Capital Gains	4,00,000

36. EXEMPTIONS AVAILABLE FOR CAPITAL GAINS ON TRANSFER OF URBAN AGRICULTURAL LAND u/s 54B

Applicability	Individual
Asset Transferred	Urban Agricultural Land used for agriculture by him or by his parents for two years immediately prior to the date of transfer.
Nature of the Asset	Long Term or Short Term Capital Asset
New Asset to be acquired	Agricultural Land
Amount to be invested in New Asset	Capital Gain on Transfer
Amount of Exemption	Least of: (a) Amount invested in New Agricultural Land, or (b) Capital Gain
Time Limit for Investment	Within Two Years from the date of transfer.
Unutilized Amount	(a) The amount not utilized before the due date of filing return shall be kept in Capital Gain Account Scheme of a Nationalized Bank. (b) The amount should be utilized within the prescribed period. (c) Amount not utilized within the prescribed period shall be treated as LTCG of the previous year in which prescribed period expires.
Holding Period of New Asset	Three Years from the date of acquisition
Sale of New Asset within holding period	Short Term Capital Gain computed as follows: Sale Consideration of New Asset Less: Cost of Acquisition reduced by Capital Gains exempted u/s 54B

Illustration 22: On 16th January 2012, Suman sold agricultural land for ₹22 lacs. He incurred selling expenses for ₹50,000. Compute capital gains :

If the land sold, was purchased on 1st February 1995 for ₹ 4 lacs, and the land was used for agricultural purposes by his mother.

He again purchased agricultural land of ₹ 8 lacs on 25th January 2012.

Amount deposited in a scheduled bank under "Capital Gains Deposit Scheme. ₹ 4 lacs on 6th April 2012.

Solution :

Computation of Capital Gains for the A.Y. 2012-13

	₹
Consideration for transfer	22,00,000
Less : Expenses on transfer	50,000
Net Consideration	21,50,000
Less : Indexed Cost of Acquisition $4,00,000 \times \frac{785}{259}$	12,12,355
Long-term Capital Gains	9,37,645
Less : Exemption u/s 54B	
Cost of New Land purchased	8,00,000
Less : Amount deposited in "Capital Gains Account Scheme" before due date of furnishing return specified u/s 139(1) ₹ 4,00,000 or the balance amount of capital gains, ₹ (9,37,645-8,00,000) = ₹ 1,37,645 whichever is less	1,37,645
Taxable long term Capital Gains	NIL

37. EXEMPTIONS AVAILABLE FOR CAPITAL GAINS ON COMPULSORY ACQUISITION OF LAND AND BUILDING USED FOR INDUSTRIAL PURPOSES u/s 54D

Applicability	All Assesses
Asset Transferred	Land and Building used by an Industrial undertaking which is compulsorily acquired and such land and building were used for business purpose during the two years before the date of transfer
Nature of the Asset	Long Term or Short Term Capital Asset
New Asset to be acquired	Land and Building for Industrial Purpose
Amount to be Invested in New Asset	Capital Gain on Transfer
Amount of Exemption	Least of: (a) Amount Invested In New Land and Building, or (b) Capital Gain
Time Limit for Investment Unutilized Amount	Within Three Years from the date of transfer. (a) The amount not utilized before the due date of filing return shall be kept in Capital Gain Account Scheme of a Nationalized Bank. (b) The amount should be utilized within the prescribed period . (c) Amount not utilized within the prescribed period shall be treated as LTCG of the previous year in which prescribed period expires .
Holding Period of New Asset	Three Years from the date of acquisition
Sale of New Asset within holding period	Short Term Capital Gain computed as follows: Sale Consideration of New Asset Less Cost of Acquisition reduced by Capital Gains exempted u/s 54D



Illustration 23 : ABC Ltd. purchased a building for an industrial undertaking on 1.1.06 for ₹5 lacs. Prior to this the company had taken this building on rent for the last 3 years and was using it for its industrial activities. There is no other building in the block. This property was compulsorily acquired by the State Government on 16.7.11 and a compensation of ₹ 7 lacs was given to the company on 31.3.012. The company purchased another building for shifting its Industrial undertaking for ₹ 4 lacs on 20th November 2012. Compute the capital gain for the assessment year 2012-13. Rate of Dep. of Building 5%.

Solution :

Computation of Capital Gains for the A.Y. 2012-13

	₹
Consideration for transfer	7,00,000
Less : Cost of Acquisition	
WDV as on 1.4.2011	3,77,218
Short term Capital Gains	3,22,782
Less : Exemption u/s 54D	
Cost of Building purchased ₹ 4 lacs	
or the short term Capital Gains ₹ 3,22,782 whichever is less	3,22,782
Taxable short term Capital Gains	NIL
Working :	
<u>W.D.V as on 1.4.11 :</u>	
Purchase price (05-06)	5,00,000
Less : Dep. for 2005-06 (less than 180 days)	
Rt. of Dep. @ 50% of 5% = 2.5% on 5,00,000	12,500
	4,87,500
Less : Dep. for 2006-07 @ 5%	24,375
	4,63,125
Less : Dep. for 2007-08 @ 5%	23,156
	4,39,969
Less : Dep. for 2008-09 @ 5%	21,998
	4,17,971
Less : Dep. for 2009-10 @ 5%	20,899
	3,97,072
Less : Depreciation for 2010-11 @ 5%	19,854
W.D.V. as on 1.4.11	3,77,218

Illustration 24: Saptarshi acquired shares of G Ltd. on 15.12.99 for ₹5 lacs which were sold on 14.6.11 for ₹ 16 lacs. Expenses on transfer of shares ₹ 20,000. He invests ₹ 8 lacs in the bonds of Rural Electrification. Corporation Ltd. on 16.10.2011.

- Compute capital gain for the assessment year 2012-13.
- State the period for which the bonds should be held by the assessee. What will be the consequences if such bonds are sold within the specified period?
- What will be the consequences if Saptarshi takes a loan against the security of such bonds.

Solution :

Computation of Capital Gains for the A.Y. 2012-13

	₹
Consideration for transfer	16,00,000
Less : Expenses on Transfer	20,000
Net Consideration	15,80,000
Less : Indexed Cost of Acquisition $5,00,000 \times \frac{785}{389}$	10,08,997
Long-term Capital Gains	5,71,003
Less : Exemption u/s 54EC	5,71,003
Taxable long-term Capital Gain	NIL

- (b) Saptarshi should not transfer or convert (otherwise than transfer) into money such bonds within 3 years from the date of their acquisition.

If these bonds are transferred or converted into money within 3 years, capital gain of ₹ 6,00,000 exempted earlier shall attract taxability towards long-term capital gain of the previous year in which such asset is transferred or converted into money.

- (c) If any loan is taken against security of such bonds, it shall be taxable as long-term capital gains of the previous year in which such loan is taken against the security of such bonds.

EXEMPTIONS FROM CAPITAL GAINS FOR INVESTMENTS IN NOTIFIED BONDS u/s 54EC

Applicability	All Assesseees
Asset Transferred	Any Long term Capital Asset
Nature of the Asset	Long Term Capital Asset
New Asset to be acquired	Bonds redeemable after 3 years issued on or after 01.04.2007 by National Highway Authorities of India (NHAI) or Rural Electrification Corporation Limited (RECL). However, deductions against these investments, once availed u/s 54EC cannot be availed u/s 80C.
Amount to be invested in New Asset	Long term Capital Gain on Transfer. Maximum amount that can be invested by the Assessee during any Financial year is ₹50 lakhs
Amount of exemption	Least of the followings: (a) Amount invested in bonds; or, (b) Capital Gains
Time limit for investment	Within six months from the date of transfer
Holding period of new asset	Three years from the date of acquisition
Sale of new asset within holding period	Long term capital gains already exempted u/s 54EC shall be charged as LTCG of the assessee in the year of sale or creation of charge on the new asset

Illustration 25 :

Anand sold a residential building at Kolkata for ₹ 25,60,000 on 1.11.2011. The building was purchased during 1979-80 for ₹ 1,45,000. FMV as on 1.4.81 ₹ 2,75,000. Brokerage paid on sales @ 2%. deposited ₹ 8 lakhs in NHAI Capital Gains Bond in February 2012. Compute Taxable Capital Gains.

Assessee: Anand

Computation of Taxable Capital Gains for the A.Y. 2012-13

Particulars	Amount (₹)
Consideration for Transfer	25,60,000
Less: Expenses on Transfer (i.e. Brokerage @ 2% on ₹25,60,000)	51,200
Net Consideration	25,08,000
Less: Indexed Cost of Acquisition = $\frac{\text{Cost of Acquisition} \times \text{CII of year of Acquisition}}{\text{CII of the year of Transfer}}$ = ₹ 2,75,000 × $\frac{785}{100}$	21,58,750
Long term Capital Gains	3,49,250
Less: Exemption u/s 54 EC Amount invested in NHAI Bonds ₹8 lakhs. Deduction restricted upto the balance of LTCG	3,49,250
Taxable Capital Gains	Nil

39. EXEMPTIONS FROM CAPITAL GAINS FOR TRANSFER OF ANY LONG TERM CAPITAL ASSET OTHER THAN A RESIDENTIAL HOUSE PROPERTY u/s 54F

Applicability	Individual / HUF
Asset Transferred	Any Long Term Capital Asset other than Residential House Property
Nature of the Asset	Long Term Capital Asset
Condition	On the date of transfer of the LTCA, the assessee should not own more than one Residential House Property
New Asset to be acquired	Residential House Property
Amount to be invested in New Asset	Net Consideration
Amount of Exemption	$\frac{\text{Long Term Capital Gain} \times \text{Amount invested in Residential House}}{\text{Net Consideration}}$
Time Limit for Investment	(a) For Purchase: Within One Year before or Two Years after the date of transfer (b) For Construction: Within Three Years after the date of transfer.
Unutilized Amount	(a) The amount not utilized before the due date of filing return shall be kept in Capital Gain Account Scheme of a Nationalized Bank (b) The amount should be utilized within the prescribed period (c) Amount not utilized within the prescribed period shall be treated as LTCG of the previous year in which the prescribed period expires
Holding Period of New Asset	Three Years from the date of acquisition or construction
Sale of New Asset within holding period	(a) Short Term Capital Gain on New Asset shall be taxed separately. (b) Long Term Capital gain exempted u/s 54F shall be chargeable to tax as Long Term Capital Gain in the year of transfer.



Illustration 26: Bipasha purchased jewellery worth ₹ 2,20,000 during 1985-86. During the year 1990-91, she further purchased jewellery worth ₹ 3,50,000. All the jewellery was sold by her on 15.6.11. The jewellery purchased in 1985-86 was sold for ₹ 20 lacs and that purchased in 1990-91 was sold for ₹ 32 lacs.

On 26.6.11 she deposited ₹50 lacs in Capital Gains Scheme account.

On 21.10.11 withdrawing from the Deposit Account, she utilised ₹ 48 lacs for purchase of a residential house property in Kolkata.

On the date of transfer she owns only one residential house.

Solution :

Computation of Capital Gains for the A.Y. 2012-13

	₹
(a) On transfer of jeweller purchased during 85-86	
Consideration for transfer	20,00,000
Less : Indexed Cost of Acquisition	
$2,20,000 \times \frac{785}{133}$	12,98,496
Long-term Capital Gains	7,01,504
(b) On transfer of jewellery purchased during 1990-91	
Consideration for transfer	32,00,000
Less : Indexed Cost of Acquisition	
$3,50,000 \times \frac{785}{182}$	15,09,615
	16,90,385

In order to avail the maximum benefit u/s 54F, the exemption should be computed as follows :

Total long-term Capital Gain (7,01,504 + 16,90,385)	23,91,889
Less : Exemption u/s 54F $\left[\frac{\text{Cost of New House} + \text{Amount Deposited} \times \text{LTCG}}{\text{Net Consideration}} \right]$	
$= \frac{50,00,000}{52,00,000} \times 23,91,889$	22,99,893
Taxable Long-term Capital Gains	91,996

Note :

1. In this case, Bipasha has not fully utilised the deposit account for acquiring a residential house property. Out of ₹ 50 lacs deposited for acquiring the house, it is utilised to the extent ₹ 48 lacs.

Tax treatment of unutilised amount, will be as follows :-

	₹
(a) Unutilised amount	2,00,000
(b) Net sale consideration	52,00,000
(c) Original Capital Gain	23,91,889
(d) Notional Long-term Capital Gain	91,996
(e) Effective exemption u/s 54F	22,07,897
[₹ 22,99,893 – 91,996]	

₹ 91,996 will be chargeable to tax as long-term capital gain after expiry of 3 years from the date of transfer of jewellery (i.e. 15.6.10). Consequently it will be taxable for the assessment year 2015-16.

2. The unutilised amount of ₹ 2 lacs can be utilised by Bipasha at any time after 15.6.11.
3. If Bipasha sells this new house property before 21.10.14, then ₹ 24,52,248 (exemption u/s 54F) will be to tax as long-term capital gain of the year in which the house is sold.
4. If Bipasha purchases another house before 15.6.13 or constructs any other house (income of which is taxable u/s 22) before 15.6.14, then ₹ 24,52,248 (exemption u/s 54F) will be deemed as long-term Capital gain of the year in which another house is purchased or constructed.

40. EXEMPTIONS AVAILABLE FOR CAPITAL GAINS ON SHIFTING OF INDUSTRIAL UNDERTAKING FROM URBAN TO RURAL AREA u/s 54G

Applicability	All Assesses
Asset Transferred	Land and Building, Plant and Machinery used by Industrial undertaking and shifting of such undertaking from Urban area to Non-urban area
Nature of the Asset	Any Capital Asset
New asset to be acquired	Land, Building, Plant and Machinery for Industrial Undertaking in Non-urban area or to meet the exoenses of shifting
Amount to be invested in New Asset	Capital Gain on Transfer
Amount of Exemption	Least of - (a) Amount invested in New Land and Building or New Plant and Machinery, or (b) Capital Gain
Time Limit for Investment	Within One Year prior to the date of transfer or within three years after the date of transfer.
Unutilized Amount	(a) Amount not utilized before the due date of filing return shall be kept in Capital Gain Account Scheme of a Nationalized Bank. (b) The amount should be utilized within the prescribed period . (c) Amount not utilized within the prescribed period shall be treated as LTCG of the previous year in which the prescribed oeriod exoires .
Holding Period of New Asset	Three Years from the date of acquisition
Sale of New Asset within holding period	Short Term Capital Gain computed as follows: Sale Consideration of New Asset Less: Cost of Acquisition reduced by Capital Gains exempted u/s 54G

Illustration 27: P Ltd. owns an industrial undertaking manufacturing chemicals in Bangalore owns the following assets

- (a) Plant and machinery (wdv ₹5 lacs) sold for ₹15 lacs.
- (b) Building (WDV ₹ 12 lacs) sold for ₹ 60 lacs.
- (c) Furniture and fixtures (WDV ₹ 50,000) sold for ₹ 1,80,000
- (d) Land cost of acquisition ₹ 5,00,000 during 1984-85 and sold for ₹ 30 lacs

The industrial undertaking was shifted as per policy of the Government from urban area to other area. The new assets acquired during the period 1.1.12 to 31.3.12 are as under:

Plant and machinery ₹20 lacs; Buildings ₹40 lacs.

Compute capital gain chargeable to tax for the assessment year 2012-13.

Solution :

Short-term Capital Gains on Depreciable assets

		₹
(i) Plant & Machinery (15,00,000 – 5,00,000)	10,00,000	
(ii) Buildings (60,00,000 – 12,00,000)	48,00,000	
(iii) Furniture & Fixtures (1,80,000 – 50,000)	<u>1,30,000</u>	59,30,000
Long-term Capital Gains on Industrial Land :		
Consideration for transfer	30,00,000	
Less : Indexed Cost of Acquisition		
$5,00,000 \times \frac{785}{125}$	<u>31,40,000</u>	<u>(1,40,000)</u>
Total Capital Gains		57,90,000
Less : Exemption u/s 54G		
Plant & Machinery	20,00,000	
Building	<u>40,00,000</u>	
	<u>65,00,000</u>	
but restricted to ₹ 56,60,000		
[= ₹ 57,90,000 — 1,30,000, being STCG on furniture, not eligible for the purpose of claiming exemption u/s 54G]		<u>56,60,000</u>
Short term Capital Gains (on furniture)		<u>1,30,000</u>

41. EXEMPTION AVAILABLE TO AN UNDERTAKING WHICH SHIFTS ITS BASE TO A SPECIAL ECONOMIC ZONE AND IN THE COURSE MAKES GAIN ON TRANSFER OF ASSET u/s 54GA

Applicability	All Assesses
Asset Transferred	(a) Land and Building, Plant and Machinery or any right in Land or Building used by Industrial undertaking. (b) Transfer as a result of shifting of such undertaking from Urban Area to Special Economic Zone (which may be situated in Urban or Any other area).
Nature of the Asset	Any Capital Asset
New Asset to be acquired	(a) Plant, Machinery for use in the Undertaking in the SEZ. (b) Acquired Land and Acquired/Constructed Building for purpose of business in SEZ (c) Shifted the undertaking to the SEZ. (d) Expenses incurred for such purposes as specified by under the Scheme by the Central Government is also eligible for claiming exemption.
Amount to be invested in New Asset	Capital Gain on Transfer
Amount of Exemption Least of :	(a) Amount invested in any Land and Building or any Plant and Machinery and Expenses incurred in relation to transfer, or (b) Capital Gain
Time Limit for Investment	Within One Year prior to the date of transfer or within three years after the date of transfer

Unutilized Amount	Amount not utilized before the due date of filing return shall be kept in Capital Gain Account Scheme of a Nationalized Bank. <ul style="list-style-type: none"> The amount should be utilized within the prescribed period. Amount not utilized within the prescribed period shall be treated as LTCG of the previous year in which the prescribed period expires.
Holding Period of New Asset	Three Years from the date of acquisition
Sale of New Asset within holding period	Short Term Capital Gain computed as follows: Sale Consideration of New Asset Less: Cost of Acquisition Less: Capital Gains exempted u/s 54GA

Illustration 28: The house property of A is compulsorily acquired by the government for ₹ 10,00,000 *vide* Notification issued on 12.3.2005. A had purchased the house in 1986-87 for ₹ 2,00,000. The compensation is received on 15.4.2009. The compensation is further enhanced by an order of the court on 15.5.2011 and a sum of ₹ 2,00,000 is received as enhanced compensation on 21.10.2011. A wants to claim full exemption of the capital gains Advise A in this respect. Compute the capital gain and determine the year in which it is taxable. Also specify the period upto which the investment in the new house should be made by the assessee.

Solution :

Although the house property is compulsorily acquired on 12.3.2005, the capital gain will arise in the previous year in which full or part of the compensation is first received *i.e.* previous year 2009-10. However, indexation will be done till the year of compulsory acquisition. Therefore, capital gains will be calculated as under :

Assessment year 2010-11		₹
Full value of consideration		10,00,000
Less :	Indexed cost of acquisition — ₹ 2,00,000 × $\frac{480}{140}$	6,85,714
Long-term capital gain		3,14,286

The assessee should either invest at least ₹ 3,14,286 for the purchase/construction of a residential house property on or before 31.7.2010 (relevant due date) and /or deposit the amount under the capital gain scheme on or before 31.7.2010, to be utilised for purchase of house property by 14.4.2011 and /or construction of the house property by 14.4.2012.

Computation of Capital Gain for the A.Y. 2012-13

		₹
Enhanced compensation Received		2,00,000
Less :	Cost/Indexed cost of acquisition	Nil
Long-term Capital Gain		2,00,000

The assessee should either invest at least ₹ 2,00,000 for the additional construction of a residential house property already acquired for claiming under section 54 on or before 31.7.2011 (relevant due date) and/or deposit the amount under the capital gain scheme on or before 31.7.2011 may invest ₹ 2,00,000 in the bonds specified under section 54EC.

42. EXTENSION OF TIME LIMIT FOR ACQUIRING NEW ASSET, WHEN ENHANCED COMPENSATION IS PAID u/s 54H

- (a) **Initial Compensation:** If initial compensation is received in parts, then the **entire initial compensation is taxable in the year in which a part is first received. Time limit for acquiring the new asset** u/s 54, 54B, 54D, 54EC and 54F shall be determined **on the basis of dates of receipt of different parts** of initial compensation.

- (b) **Enhanced Compensation:** If any enhanced compensation is received, it is **taxable in the year in which such compensation is received** and for **acquiring the new asset** u/s 54, 54B, 54D, 54EC and 54F, the time limit shall be determined **from the date of receipt of additional (enhanced) compensation**.

43. PROVISIONS RELATING TO CLAIMING OF EXEMPTION IN ORDER TO REDUCE TAX LIABILITY ON SHORT TERM CAPITAL GAINS

Exemption u/s	Applicable for
54B	Transfer of Agricultural Land
54D	Transfer by way of Compulsory acquisition by Government
54G	Shifting of Industrial Undertaking from Urban to Rural Area
10(37)	Compulsory acquisition of Agricultural Land by Central Government/RBI.
10(41)	Transfer by Companies engaged in Power Sector Business

44. COST IN RELATION TO CERTAIN FINANCIAL ASSETS u/s 55

	Particulars of asset	Date of Acquisition Holding	Cost of Acquisition Period
1.	Shares originally purchased :		
(a)	Primary market	Date of Allotment	Allotment price
(b)	Secondary market		
(i)	Transactions through share brokers	Date of broker's note	Amount paid + Brokerage Charges + Adjustment for ex. & cum. dividend/ interest
(ii)	Transactions between parties directly	Date of contract of sale	As above (excluding Brokerage)
2.	Shares acquired in different lots at different Doints of time	FIFO method	FIFO method
3.	Shares held in depository system (taxable in hands of beneficial owner)	FIFO Method	FIFO Method
4.	Right shares offered to existing shareholders and subscribed by him	Date of allotment	Offer Price
5.	Right shares acquired by a person by way of renouncement	Date of allotment	Offer Price + Amount paid for renouncement
6.	Renouncement of right shares in favour of another person	Holding period is date of offer of such right to the date of renouncement (always STCG)	NIL
7.	Financial asset acquired without any payment/consideration.	Date of allotment of such financial assets	NIL

Other Points :

1. Splitting of shares is not a transfer.
2. Debentures and Bonds are not entitled for benefit of Indexation u/s 48.

45. "DIVIDEND STRIPPING" enforced by Section 94(7) of the Income-tax Act, 1961.

1. **Purchase:** The securities or units are purchased within 3 months prior to the record date.
2. **Sale:** Sale or transfer is done within –
 - (a) 3 Months for Securities, and
 - (b) 9 Months for Units, after the record date.
3. **Exempt Income:** Dividend / Income on such securities/units Is exempted from tax.
4. **Dividend Stripping :** Loss arising out of such purchase and sale is ignored to the extent of dividend income.



5. Record Date means such date as fixed by

- A Company for the purposes of entitlement of the holder of the securities to receive dividend.
- A Mutual Fund or the Administrator of the Undertaking / Company specified u/s 10(35) Explanation, for the purposes of entitlement of the holder of the units to receive income or additional units, without any consideration.

46. BONUS STRIPPING: Section 94(8):

1. Applicability: All Assesses

2. **Transaction:** Any person who purchases Units (Original Units) within a period of 3 months prior to record date and sells such units within a period of 9 months after such record date. On the record date, he was allotted Bonus Units (additional units without any payment)

3. Tax Implication:

- The loss on sale of such original units shall be ignored for the purpose of computing his income.
- Loss so ignored will be deemed as the Cost of Acquisition of such additional units, on their subsequent sale/transfer.

47. RATES OF CAPITAL GAIN TAX - SECTION 112

- Short-term capital gain** is taxed at normal rate. In respect of Listed Securities transferred on or after 1.10.2005, Section 111A will apply i.e. taxable at 10%.
- Long-term capital gain other than gains arising out of transfer of security including Zero Coupon Bonds are taxed as follows :**

Kind of Assessee	Tax %
(a) Individual and HUF Resident Non-Resident [not covered in (d)]	20% 20%
(b) Venture capital company on transfer of equity shares of venture capital undetaing	20%
(c) Company [not covered in (b)] Domestic Company Foreign Company (not covered in (d))	20% 20%
(d) Offshore funds Non-resident assesses, foreign institutional investors covered by Sections 115AB/115AC/115AD	15%
(e) Any others (Firm, AOP, BOI etc.) • Resident • Non-Resident [not covered in (d)]	20% 20%

Note : The rates given above are Basic Rates. Appropriate Surcharge, Education Cess and Secondary and Higher Education Cess are also applicable in addition to the tax rate mentioned above.

3. Long-term capital gain arising from transfer of security listed in a Recognized Stock Exchange, not covered by Securities Transaction Tax:

- Compute capital gain **without indexation** and charge tax @ 10%.
- Compute capital gain **with indexation** and charge tax @ 20% as per Section 112
- The assessee has the option to choose either of the above whichever is beneficial to him.
- Long Term Capital Gain arising on listed securities being Equity Shares and Units of Equity Oriented

Notes :

- No deduction** shall be allowed **under Chapter VIA** in respect of income from long-term capital gain.
- Special Benefit for Resident Individuals HUF: Applicability:** Resident Individual or Resident HUF
Condition: Total income excluding Long-Term Capital Gains Is **less than the basic exemption. Benefit:**

Tax on Long-Term Capital Gain Is determined as follows–

Tax on LTCG = 20% [Total Income including LTCG - Basic Exemption]

Only that amount of long-term capital gains which is included in the total income would be Cir. No. 721/13.9.95 subject to tax at a prescribed flat rate u/s 112.

4. Tax on Short Term Capital Gain on Listed Securities - Section 111A (w.e.f. 1.10.2005)

- (a) **Applicability:** All Assesses
- (b) **Source of Income:**
 - Income from Short Term Oriented Fund.
 - The transfer has been affected on or after 1.10.2005
 - Such transaction is liable for Securities Transaction Tax.
- (c) **Rate of Tax:** 10% of Short-term Capital Gains

Notes :

- (a) Chapter VI-A deduction shall not be allowed in respect of income from such Short Term Capital Gain.
- (b) **Special Benefits for Resident Individuals or Resident HUF: Applicability:** Resident Individual or Resident HUF **Condition:** Total income excluding Short -Term Capital Gains is less than the basic exemption.

Benefit: Tax on Short-Term Capital Gain is determined as follows:

Tax on STCG = 10% [Total Income including STCG - Basic exemption]

Funds, transferred on or after 1.10.2005 is exempt from tax u/s 10(38).

48. Set off and carry forward of losses under the head Capital Gains.

1. Treatment for Current Year Loss: (Section 70 &. 71)

- (a) **Current year Short Term Capital Loss** can be **set off against any capital gain** accrued during, the previous year, but It **cannot be set off against income under any other head.**
- (b) Current year Long Term Capital Loss shall be **set off only against Long Term Capital Gains.**

2. Treatment for Carry Forward Loss: (Section 74)

- (a) **Unabsorbed Loss** under the head Capital Gains shall be **carried forward** for a period of 8 **Assessment Years** immediately following the Assessment Year in which such loss was incurred.
- (b) The **carry forward short-term** capital loss can be set off **against any capital gains.**
- (c) The **carry forward Long Term Capital Loss** can be set off **only against Long Term Capital Gains.**



STUDY NOTE - 8

INCOME FROM OTHER SOURCES

This Study Note includes

- **Various Provisions of the Income Tax Act for determination of income under the head “Income from other sources”**

8.1 INCOME FROM OTHER SOURCES - BASIS OF CHARGE [Sec. 56]

This is the residual head of charge of income. Where a source of income does not specifically fall under any one of the other heads of income viz. Salaries, Income from House Property, Profits and Gains of Business or Profession, Capital gains, such income is to be brought to charge under sec. 56 under the head ‘Income from other sources’- S.G. Mercantile Corp. P. Ltd. v. CIT 83 ITR 700(SC).

This residuary head of income would be invoked only if all the following conditions are fulfilled

1. There is a taxable income- Sec. 2(24) read with Sec. 4 & 5
2. The income is not exempt from tax under - Sec. 10 to 13A
3. Income should not fall under any of the four specific heads of income viz. salaries, income from House Property, Profits and gains of Business or Profession and capital gains.

8.2 CHARGEABLE INCOME [Sec. 56(2)]

As per Sec. 56(2), the following incomes are expressly stated to be chargeable to tax under the head “Income from other sources”—

- (i) Dividend [Sec. 56 (2) (i)]
- (ii) Any winnings from lotteries, crossword puzzles, races including horse races, card games and other games of any sort or form, gambling or betting of any form or nature whatsoever- [Sec. 56(2)(ib)]
- (iii) Any sum received by assessee from his employees as contributions to any provident fund or superannuation fund or any fund set up under the provisions of the Employees’ State Insurance Act, 1948 or any other fund for the welfare of the employees, if such income is not chargeable under the head “Profits and gains of Business or Profession”- [Sec. 56(2)(ic)].
- (iv) Income by way of interest on securities, if it is not chargeable as Profits and gains of business i.e. where securities are held as investments- Sec. 56(2)(id).
- (v) Income from machinery, plant or furniture belonging to the assessee let on hire, if the income is not chargeable to income-tax under the head, Profits and gains of Business or Profession - Sec. 56(2)(ii).
- (vi) Income from letting of machinery, plant or furniture, if such income is not chargeable under the head “Profits and gains of Business or Profession”- Sec. 56(iii)
- (vii) Any sum received under “Key man insurance policy including bonus, if not charged under the head “Profits and gains of Business or Profession”- Sec. 56(iv)
- (viii) Gifts aggregating to more than ₹ 50,000 in a year on or after 1st Day of April, 2006 - Sec. 56(vi)
- (ix) **Taxation of property acquired without consideration or for an inadequate consideration as ‘income from other sources’ (Section 56(2)(vii)) [W.e.f. 1-10-2009]**

Section 56(vi) provides that any ‘sum of money’ (in excess of the prescribed limit of ₹ 50,000) received without consideration by an individual or HUF will be chargeable to income tax in the hands of the recipient under the head ‘income from other sources’.

However, receipts of money (a) from relatives or (b) on the occasion of marriage or (c) under a will or inheritance or (d) in contemplation of death of payee or donor are outside the scope of the provisions of section 56(2)(vi) of the Income-tax Act.

Similarly, anything which is received in kind having 'money's worth' i.e. property is also outside the purview of the existing provisions.

The Act has amended section 56 of the Income-tax Act by inserting a new clause (vii) to section 56(2) w.e.f. 1-10-2009 to provide that the value of any property received without consideration or for inadequate consideration will also be included in the computation of total income of the recipient. Such properties will include: (i) immovable property being land or building or both, (ii) shares and securities, (iii) jewellery, (iv) archaeological collections, (v) drawings, (vi) paintings, (vii) sculptures (viii) any work of art.

In a case where an immovable property is received without consideration and the stamp duty value of such property exceeds ₹ 50,000, the whole of the stamp duty value of such property shall be taxed as the income of the recipient. If an immovable property is received for a consideration which is less than the stamp duty value of the property and the difference between the two exceeds ₹ 50,000 (inadequate consideration), the difference between the stamp duty value of such property and such consideration shall be taxed as the income of the recipient.

If the stamp duty value of immovable property is disputed by the assessee, the Assessing Officer may refer the valuation of such property to a Valuation Officer. In such cases, the provisions of existing section 50C and section 155(15) of the Income-tax Act shall, as far as may be, apply for determining the value of such property.

In a case, where movable property is received without consideration and the aggregate fair market value of such property exceeds ₹ 50,000, the whole of the aggregate fair market value of such property shall be taxed as the income of the recipient. If a movable property is received for a consideration which is less than the aggregate fair market value of the property and the difference between the two exceeds ₹ 50,000, the difference between the fair market value of such property and such consideration shall be taxed as the income of the recipient.

It has also been provided that :

- (i) The value of moveable property shall be the fair market value as on the date of receipt in accordance with the method prescribed; and
- (ii) In the case of immovable property, the value of the property shall be the 'stamp duty value' of the property.
- (iii) 'Relative' shall have the meaning assigned to it in the Explanation to clause (vi) of section 56(2).

Further, section 56(2)(vii) shall not apply to any sum of money or any property received—

- (a) from any relative; or
- (b) on the occasion of the marriage of the individual; or
- (c) under a will or by way of inheritance; or
- (d) in contemplation of death of the payer or donor, as the case may be; or
- (e) from any local authority as defined in the Explanation to clause (20) of section 10; or
- (f) from any fund or foundation or university or other educational institution or hospital or other medical institution or any trust or institution referred to in clause (23C) of section 10; or
- (g) from any trust or institution registered under section 12AA.

Related amendments :

1. Section 2(24) relating to definition of income amended: The Act has inserted clause (xv) to section 2(24) to provide that any sum of money or value of property referred to in section 56(2)(vii) shall also form part of income.
2. Cost of disquisition of the property required in a manner given under section 56(2)(vii): The Act has inserted sub-section (4) to section 49 to provide that where the capital gain arises from the transfer of a property, the value of which has been subject to income-tax under section 56(2)(vii), the cost of acquisition of such property shall be deemed to be the value which has been taken into account for the purposes of the said clause (vii).



- (x) **Interest received on delayed compensation or enhanced compensation shall be deemed to be income of the year in which it is received (Section 56(2)(viii), section 57(iv) and section 145A] (W.e.f. A.Y. 2010-11]**

The existing provisions of Income-tax Act provide that 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. Further, the Hon’ble Supreme Court, in the case of *Rama Bai vs. CIT* (1990) 181 ITR 400 (SC) has held that arrears of interest computed on delayed or enhanced compensation shall be taxable on accrual basis. This has caused undue hardship to tax payers.

With a view to mitigating the hardship, the following changes have been made in this regard :

- (1) Clause (b) to section 145A inserted: The Act has amended section 145A to provide that the interest received by an assessee on compensation or 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.
- (2) Interest on compensation or on enhanced compensation to be taxed under other sources: Clause (viii) in sub-section (2) of section 56 has been inserted to provide that income by way of interest received on compensation or on enhanced compensation referred to in sub-clause (b) of section 56 shall be assessed as “income from other sources” in the year in which it is received.
- (3) 50% deduction to be allowed from such interest: Clause (iv) has been inserted to section 57 to provide that in the case of income of the nature referred to in section 56(2)(viii), a deduction of a sum equal to 50% of such income shall be allowed and no deduction shall be allowed under any other clause of this section.

Some important items of income stated above are hereunder discussed :

DIVIDEND [Sec. 56(2)(i)]

Dividend means the sum paid to or received by a shareholder proportionate to his shareholding in a company out of the total sum distributed. The definition of “Dividends” under section 2(22) is an inclusive definition and it means dividend as normally understood and include in its connotation several other receipts set out in the definition- *Kantilal Manilal vs. CIT* 41 ITR 275(SC).

The term “Dividends” includes deemed dividends of the following nature :

- (i) Any distribution of accumulated profits entailing the release of company’s assets- Sec. 2(22)(a).
- (ii) Any distribution of debenture stock, deposit certificates to shareholders and bonus to preference shareholder- Sec. 2(22)(b).
- (iii) Any distribution to shareholders on liquidation of company to the extent to which the distribution is attributable to the accumulated profits of the company, other than distribution in respect of any share issued for full cash consideration where the shareholder is not entitled to participate in the surplus assets in the event of liquidation- Sec. 2(22)(c).
- (iv) Any distribution on reduction of share capital to the extent to which the company possesses accumulated profit except a distribution in respect of any share issued for full cash consideration where the shareholder is not entitled to participate in the surplus asset in the event of liquidation — Sec. 2(22)(d).
- (v) Any payment by way of advance or loan by a closely held company following :
 - (a) a shareholder, being a person who is the beneficial owner of shares (other than shares entitled to a fixed rate of dividend) holding not less than 10% of voting power; or
 - (b) any concern in which such shareholder is a member or partner and in which he has a substantial interest; or
 - (c) a person acting on behalf or for the individual benefit of any such shareholder - Sec. 2(22)(e)]

Note :

- (i) An advance or loan to a shareholder of the said concern in the ordinary course of the business of the company where the lending of money is a substantial part of the company’s business will not be regarded as dividend.

- (ii) Any payment made by a company on purchase of its own shares from a shareholder in accordance with sec. 77A of the Companies Act, 1956, is not treated as dividend.
- (iii) Distribution of shares by the resulting company to the shareholder of the demerged company is also not to be treated as dividend.

DIVIDEND EXEMPT

- (i) Dividend declared/distributed/paid by domestic company including deemed dividend (i.e. other than the dividend u/s. 2(22)(e) or dividend from a foreign company) is exempt in the hands of shareholder. However, the company has to pay dividend distribution tax on it under section 115-O [Sec. 10(34)]
- (ii) any dividend : (a) on units of a Mutual Fund specified under clause (23D); or (b) in respect of units from the Administrator of the specified undertaking; or (c) in respect of units from the specified company [Sec. 10(35)]

EMPLOYEES' CONTRIBUTIONS TO PROVIDENT FUND ETC, [Sec. 56(2)(ic)]

It has to be remembered that any sum received by the assessee from his employees as contributions to any provident fund or superannuation fund or any fund set up under the provisions of the Employees' State Insurance Act, 1948 or any other fund for the welfare of such employees is income in the hands of the assessee and is chargeable as income from other sources if not chargeable as Profits and gains on Business or Profession [Sec. 2(24)(x)]

However, the tax payer is entitled to deduction of the sum of such contributions received from his employees if such sum is credited by the taxpayer to the employee's account in the relevant fund on or before the due date. Here, the due date means the date by which the assessee is required as an employer to credit an employees' contribution to the employees' account in the relevant fund under an Act, rule, etc. issued in that behalf [Sec. 36(1)(va)].

Therefore, any sum received by the assessee from his employees as contributions to any fund as aforesaid and is not deposited or deposited belatedly to the employee's account, it becomes income of the assessee.

INTEREST ON SECURITIES

Interest on securities is chargeable as income from other sources if it is not chargeable as Profits and gains of Business or Profession, i.e. when the securities are held as investment.

- (a) **Basis of Charge** – If the books of account are maintained on cash basis the interest on securities will be chargeable on receipt basis. However, where books of account are maintained on mercantile system or where no method of accounting is regularly employed by the assessee, such interest will be chargeable on "accrual basis" i.e. as the income of the Previous Year in which such interest is due to the assessee – second proviso to sec. 145(1).
- (b) **Interest on securities exempt** – The interest on securities of the following description is exempt from tax –
 - (i) interest on notified securities, bonds or certificates issued by the Central Govt.
 - (ii) interest to an individual or a HUF on 7% Capital investment Bond or on notified Relief Bonds.
 - (iii) interest to non-resident Indians on notified bonds.
 - (iv) interest on securities held by issue Department of the Central Bank of Ceylon.
 - (v) Tax planning - Taxpayer is entitled to the deduction of any reasonable sum paid as commission or remuneration to a banker or any other person for the purpose of realizing interest on securities. Similarly, he will also be entitled to the deduction of interest on capital borrowed for investing in securities.

INCOME FROM INSEPARABLE LETTING OF MACHINERY, PLANT OR FURNITURE WITH BUILDING

If an assessee lets on hire machinery, plant or furniture and also buildings and the letting of building is inseparable from the letting of machinery, plant or furniture, the income from such letting would be chargeable to tax under the residuary head where it is not chargeable under the 'Profits and gains of Business or Profession'.

What is therefore, necessary to examine is whether the letting is by way of business. Whether a particular letting is of business has to be decided in the circumstances of each case. Each case has to be looked at from a businessman's point of view to find out whether the letting was the doing of business or the exploitation of his



property by the owner. A commercial asset is only an asset used in a business and nothing else, and business may be carried on with practically all things. Therefore, it is not possible to say that a particular activity is business because it is concerned with an asset with which trade is carried on- Sultan Bros. (P) Ltd. vs. CIT (1964) ITR 353 (SC).

Example : Mr. A let out his building along with air conditioning plant, tube-wells, refrigerators, etc. Though separate rent is fixed in the lease deed refers to them collectively as “demised premise”, it will be a case of inseparable letting and the entire rental income will be assessable as income from other sources.

GIFT

Now gift received during the previous year shall be included in the income if the aggregate of the gifts received exceeds ₹ 50,000.

However, the following gifts are not included in taxable income, viz.

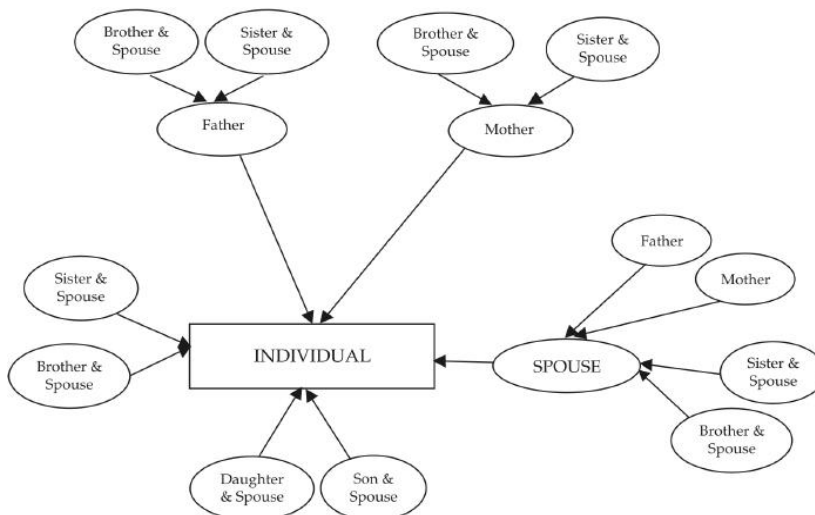
- from any relative; or
- on the occasion of the marriage of the individual; or
- under a will or by way of inheritance; or
- in contemplation of death of the payer; or
- from any local authority as defined in the Explanation to clause (20) of section 10; or
- from any fund or foundation or university or other educational institution or hospital or other medical institution or any trust or institution referred to in clause (23C) of section 10; or
- from any trust or institution registered under section 12AA.

For this purposes of this clause, “relative” means—

- 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 the person referred to in clauses (ii) to (vi).

In respect of gifts from relatives, although exempt from tax, in respect of income earned from such a gift, provisions relating to clubbing of income apply in certain cases e.g. gift received from spouse and father-in-law.

GIFT FROM THE FOLLOWING RELATIVES IS TAX FREE



OTHER INCOMES INCLUDEBLE UNDER THE HEAD

- Apart from the incomes specified in Sec. 56(2) of the Act, as mentioned above, courts have held that incomes of the following nature will be chargeable as income from other sources:
- Income of company in winding-up. *Vijay Laxmi Sugar Mills Ltd. v. CIT*
- Gratuity received by a director who is not an employee of the company. *CIT v. Lady Navajbai R.J. Tata*
- Interest is assessed under the head 'Income from other sources', if it not taxed as business or professional income. *CIT v. Govinda Choudhury & Sons* .
- Interest on tax refunds *Smt. B. Seshamma v. CIT*
- Interest earned prior to commencement of business - *CIT v. Modi Rubber Ltd. / Goa Carbon Ltd. v. CIT*
- Interest earned on short-term investment of funds borrowed for setting up of factory during construction of factory before commencement of business has to be assessed as income from other sources and it cannot be held to be non-taxable on ground that it would go to reduce interest on borrowed amount which would be capitalized - *Tuticorin Alkali Chemicals & Fertilizers Ltd. v. CIT*.
- Tax on salary of assessee borne by payer, for whom assessee was working under a contract, under a legal obligation - *Emil Webber v. CIT*
- Sale receipts prior to commencement of business *CIT v. Rassi Cement Ltd.*
- If the business as a whole is let out the income i.e. the rent, would not be liable to be assessed as income from business. If only the commercial assets are leased out the income would continue to be income from business- *CIT Vs. Biswanath Roy, CIT Vs. Kuya & Khas Kuya Colliery Co.*
- Reimbursement of taxes on salary – *Z. Zizlaw Skakuz Vs. CIT*
- Interest on employee's contribution to unrecognised provident fund- *CIT vs. Hyatt*
- Interest on bank deposits of idle business funds - *Collis Line P. Ltd. Vs. ITO*
- Interest deposit of share capital in bank before commencement of business *Traco Cable Co. Ltd. vs. CIT*
- Interest on realizations put by liquidator of company in fixed deposits- *Vijay Lakshmi Sugar Mills Ltd. vs. CIT*
- Interest received from Government u/s. 214/243/244/244A of the Income Tax Act, 1961- *Smt. B. Seshmma vs. CIT*
- Income from subletting of a House Property by a tenant.
- Insurance commission, if it is not assessable as income from business.
- Family Pension
- Director's Sitting Fees for attending board meeting
- Income from undisclosed sources
- Income received after discontinuance of business
- Examinorship fee received by a teacher.

INCOME NOT CHARGEABLE UNDER RESIDUARY HEAD

Income of the following nature will not be chargeable as income from other sources but on business income –

- I. Interest on short-term deposit with State Bank received by a cooperative society carrying on banking business- *Bihar State Cooperative Bank Ltd. Vs. CIT*
- II. Income to the principal from business carried on through an agent- *CIT vs. S.K. Sahana and Sons Ltd.*
- III. Portion of business received by beneficiary from trust or wakf-*CIT vs. P. Krishna Warier.*
- IV. Income from temporary letting out of business assets as a part of exploitation is to be assessable as business income and not as income from other sources- *CIT vs. Vikram Cotton Mills Ltd.*

INCOME FROM LETTING OF MACHINERY, PLANT OR FURNITURE

The income from machinery, plant or furniture belonging to the assessee and let out on hire is chargeable as income from other sources, if it is not chargeable as Profits and gains of Business or Profession. - Sec. 56 (2) (ii).

**DEDUCTIONS [Sec. 57]**

The income chargeable under the head “Income from other sources” shall be computed after the following deductions, namely –

- (a) In the case of dividend income and interest on securities—
 - (i) Any reasonable sum paid by way of remuneration or commission for the purpose of realizing dividend or interest, and
 - (ii) interest on borrowed capital if required for investment in shares or securities.
- (b) In the case of income from machinery, plant or furniture let on hire
 - (i) current repairs to building - sec. 30(a)(ii)
 - (ii) current repairs to machinery, plant or furniture and insurance premium -sec.(31)
 - (iii) depreciation on building, machinery, plant or furniture - sec. (32) subject to sec.38 and
 - (iv) unabsorbed depreciation - sec. 32(2).
- (c) In the case of income in the nature of family pension- ₹ 15,000 or 33.33% of such income whichever is less.
- (d) In the case of income specified in sec. 2(24)(x) i.e. deductions from employee salary for any fund, expenses of nature specified in – S. 36(1)(va) i.e. contribution to such fund on or before the due date.
- (e) Any other expenditure (not being a personal or capital expenditure) expended wholly and exclusively for the purpose of earning such income. However, this deduction is not available to a foreign company in respect of dividend income.

AMOUNTS NOT DEDUCTIBLE [Sec. 58]

The following amounts are not deductible while computing income from other sources—

- Personal expenses of the assessee – Sec. 58(1)(a)(i)
- Interest payable outside India on which tax has not been paid or deducted at source S.58(1)(a)(ii)
- Salary payable outside India on which no tax has been paid or deducted at source – Sec. 58(1)(a)(iii)
- Any sum paid on account of wealth tax- sec. 58(1A).
- any expenditure referred to sec. 40A i.e. excessive payment to relatives u/s. 40A(2) & 20% of cash payment where it exceeds ₹ 20,000 u/s. 40A(3).

Enhancement of limit for disallowance of expenditure made otherwise than by an account payee cheque or account payee bank draft for plying, hiring or leasing goods carriages in the case of transporters to ₹ 35,000 from the existing limit of ₹ 20,000 (Section 40A(3) and (3A) | (applicable to transactions effected on or after 1-10-2009)

The existing limit for other categories of payments will remain at ₹ 20,000 subject to the exceptions declared in Rule 6DD of the Income-tax Rules.

- Where an assessee has income from other sources no deduction of any expenditure or allowance in connection with such income shall be allowed under any other provisions of the Act in computing the income by way of any winnings from lotteries, crossword puzzles, races including horse races, and games – S.58(4). However, this prohibition will not apply to the owner of the horse maintained by him in horse race in computing his income from the activity of owning and maintaining such horses – Proviso to Sec. 58(4).

PROFITS CHARGEABLE TO TAX [Sec. 59]

Where an allowance or deduction has been made in the assessment for any year in respect of loss, expenditure or trading liability incurred by the assessee and subsequently during any previous year he has obtained any amount or benefit in any form in respect of such loss or expenditure or trading liability the amount or value of benefit obtained by such person shall be deemed to be income from other sources. If any amount or benefit is obtained by a successor it shall be chargeable to income-tax as income of such a successor.

In short, provision of sec. 41(1) of the Act are made applicable while computing the income of an assessee under the head income from other sources, as they apply in computing the income of an assessee under the head 'Profits and gains of Business or Profession'.

METHOD OF ACCOUNTING [Sec. 145]

Income chargeable under the head "Income from other sources" shall be computed in accordance with cash system of accounting or mercantile system of accounting regularly employed by the assessee.

Exception to this general rule is deemed dividend income covered by sub-clause (e) of clause (22) of section 2 which is chargeable to tax on payment basis as prescribed under section 8 of the Income-tax and not on the basis of method of accounting followed.

Points to be noted:

- (i) An assessee is entitled to change his regular method of accounting by another regular method and such change can be effected in respect of apart of assesses income.- Snow White Food Products Co Ltd. v/s CIT
- (ii) Where assesses is allowed to change his method of accounting from an accounting year he is entitled to claim computation of income on changed basis.- Seth Chemical Works v/s CIT
- (iii) A company was regularly valuing its stock under total cost method and wanted to change the method of valuation which excluded certain expenses which were to be included under former method. The company allowed to change method. CIT v/s Carborandum Universal Ltd.
- (iv) Mere circumstances that appellant should dividend income under this head in its return could not in law decide nature of dividend income. Brooke Bond & Co Ltd. v/s CIT- SC.

QUESTIONS & ANSWERS ON INCOME FROM OTHER SOURCES

Question 1. A Company, incorporated for the manufacture of steel, had not commenced production. The plant and machinery was in the stage of erection. During the previous year ending 31.3.2010, it paid interest on borrowings, amounting to ₹20 Lakhs. It also received interest of ₹ 1.50 Lakhs on investment in Short-Term deposits of moneys not immediately required for business. The Assessing Officer assessed the interest income under other sources. Discuss the correctness of the assessment.

Answer :

- (a) Interest on surplus funds: Interest income earned on deposits made out of surplus funds before commencement of business is taxable as "Income from other sources".
- (b) In view of the above judgement, the sum received as interest on deposits shall be charged to tax under the head 'Income from Other Sources'.
- (c) No part of the interest paid on the loan borrowed shall be allowed as deduction u/s 57 as the same was not borrowed wholly and exclusively for the purpose of earning such interest. Whole of such interest shall be capitalised.
- (d) Therefore, the action of the Assessing Officer is correct.

Question 2. A Chartered Accountant handles the moneys belonging to his clients and maintains a separate account for these moneys. Part of these moneys, In excess of current requirements, is kept in deposit on which interest is earned. The Assessing Officer proposes to assess the interest income in the hands of the Chartered Accountant. How would you contest the action of the Assessing Officer?

Answer :

- (a) Under the Chartered Accountants Act, 1949, a Chartered Accountant has to keep the monies belonging to a client in a separate bank account. He holds these funds only in a fiduciary capacity. Therefore, the Chartered Accountant cannot make use of such monies for his own benefit.
- (b) The beneficial interest in the monies so deposited in a separate bank account lies with the owner of the funds, i.e. the clients. Therefore, the interest accrued on such funds also belongs to the clients.
- (c) In view of the above, the interest do not accrue in the hands of the Chartered Accountant and hence not chargeable to tax in his hands.
- (d) Therefore, action of the Assessing Officer is not correct.



Question 3. Discuss the correctness or otherwise of the following proposition: Kumar took part in a motor-car rally and is awarded a prize money of ₹ 10,000 for winning a race. He claims that the amount of ₹ 10, 000 is exempt from tax.

Answer :

- (a) Winnings from motorcar rally are a return for skill and endurance. It is taxable as income.
- (b) In view of the above Supreme Court ruling, the amount of ₹10,000 won by Mr. Kumar shall be treated as income and chargeable to tax under the head Income from Other Sources.
- (c) Therefore, contention of Mr. Kumar is not correct and valid in law.

Question 4. Discuss the taxability of gifts received by an Assessee.

Answer :

1. Applicability: Gifts received by Individual and HUF irrespective of Residential Status.
2. Taxability: Any sum of **money, aggregate value of which exceeds ₹50,000**, is received during the previous year without consideration, by an Individual or a HUF from any person(s) on or after 1.4.2007, then the **whole of the aggregate of such sum** will be taxable.
3. **Exceptions:**
 - (a) Gifts received from the following persons not taxable -
 - From a relative, or
 - On the occasion of the marriage of the individual, or
 - Under a will or by way of inheritance, or
 - In contemplation of death of the payer, or
 - Any Local Authority, or Fund/Foundation/University/Educational Institution or Hospital or
 - other Medical Institution or
 - Trust or Institution referred u/s 10(23C), or
 - Trust / Institution registered u/s 12AA
 - (b) Gifts received in kind not taxable.
4. **Relative means:**
 - (a) Spouse of the individual,
 - (b) Brother or sister of the individual,
 - (c) Brother or sister of the spouse of the individual,
 - (d) Brother or sister of either of the parents of the individual,
 - (e) Any lineal ascendant or descendant of the individual,
 - (f) Any lineal ascendant or descendant of the spouse of the individual,
 - (g) Spouse of the person referred to in clauses (b) to (f) above.

Question 5. B an individual, gets ₹70,000 as a birthday gift from his Grandfather. Is the receipt taxable under the Income Tax Act?

Answer : B has received the gift from his grandfather. Grandfather is a relative. Hence, the receipt is not taxable.

Question 6. Discuss the taxability or otherwise of the following gifts received by H, an individual, during the Financial Year 2009-10:

- (a) ₹ 25,000 each from his four friends on the occasion of his birthday.
- (b) Wrist watch valued at ₹ 40,000 from his friend.

Answer:

- (a) ₹1,00,000 (i.e. ₹ 25,000 × 4) from his four friends on the occasion of his birthday, is taxable as income from other sources, since friends are not relatives and the amount has exceeded ₹ 50,000.

(b) Gift in kind is not taxable. Hence, wrist watch of ₹40,000 received as a gift from friend is not taxable.

Question 7. Fiona received the following gifts during the year ending 31.03.2010:

- (a) ₹ 40, 000 from her elder sister.
- (b) ₹60,000 from the daughter of her elder sister.
- (c) ₹ 1,25,000 from various friends on the occasion of her marriage,

Discuss the taxability or otherwise of these gifts in the hands of Fiona.

Answer :

- (a) ₹40,000 received from elder sister, is not taxable, as elder sister is a relative.
- (b) ₹60,000 received from the daughter of her elder sister, is taxable, as the donor, in this case, is not a relative as per the definition of the Act.
- (c) ₹1,25,000 is not taxable as it is received on the occasion of her marriage.

Question 8. Discuss the taxability of Family Pension.

Answer :

Family pension means pension received by the family members of the deceased employee.

It is chargeable to tax under the head 'Income from Other Sources'.

Deduction u/s 57: Least of the following is allowed as a deduction -

- (a) 33 1/3 % of gross pension
- (b) ₹15,000

Exemptions :

- (a) Family pension received by family members of Army personnel who are recipient of gallantry awards [Section 10(18)].
- (b) Family pension received by the widow or children or nominated heirs of a member of the armed forces (including para-military forces) whose death has occurred in the course of operational duties [Section 10(19)].

Question 9. V. G. had placed a deposit of ₹ 10 Lakhs in a bank on which he received interest of ₹80, 000. He had also borrowed ₹5 Lakhs from the same bank on the security of the deposit and was liable to pay ₹50,000 by way of interest to the bank. He therefore offered the difference between two amounts of ₹30,000 as income from other sources. Is this correct?

Answer :

- (a) U/s 57, any expenditure (not being capital expenditure) expended to earn income chargeable under the head "Income from Other Sources" will be allowed as deduction against such income.
- (b) Interest on bank FD was the income in the hands of the assessee and the interest on the loan taken from bank on that deposit is not an allowable expenditure.

Therefore, in the given case, the interest of ₹50,000 paid by VG is not allowable as deduction, and the entire interest of ₹80,000 is fully taxable.

Question 10. Shrey purchased in 2003, 10,000 Shares of Hero Ltd. for ₹5 Lakhs by borrowing money from a bank. He holds them as 'Investments'. He received dividend during the previous year 2011-12. He has paid interest of ₹85,000 on the loan to the bank during the previous year. Please advise Shrey, how should he deal with these facts in computing his income?

Answer :

- (a) In computation of total income under the Income Tax Act, the expenditure incurred in relation to income, which does not form part of Total Income, shall not be allowed as deduction. [Section 14A]
- (b) Dividend Income is exempt u/s 10(34) and hence does not form part of Total Income.

Therefore, the interest payment is not an allowable expenditure.

Question 11. Mr JK gets the following gifts during the previous year 2011-2012.

	Date of gift	Name of the donor	Amount of gift (₹)
1.	01.07.2011	Gift from R, a friend, by cheque	50,000
2.	01.09.2011	Cash gift from N, nephew	1,00,000
3.	01.12.2011	Gift of diamond ring on his birthday, by a friend, C	75,000
4.	15.12.2011	Cash gifts of ₹ 31,000 each made by four friends on the occasion of his marriage	1,24,000
5.	21.12.2011	Cash gift made by wife's sister on house opening ceremony	51,000
6.	15.01.2012	Cash gift from a close friend of father-in-law.	1,51,000
7.	31.01.2012	Cash gift made by great-grandfather	1,51,000
8.	01.02.2012	Cash gift received under the Will of a friend, who is seriously ill.	51,000
9.	15.02.2012	Cash gift made by a business friend on his birthday	75,000
10.	31.03.2012	Cash gifts made by three friends of ₹ 25,000 each	

Besides this, JK is engaged in the business of sale and purchase of retail goods. He maintains no account books. Gross turnover from retail trading is ₹ 35,00,000. Compute his total income for the assessment year 2012-2013.

Solution : Computation of taxable income for the AY 2012-2013

Particulars	Amount (₹)
1. Income from retail trading business [Sec. 44 AF] 5% ₹ 35,00,000	1,75,000
2. Income from other sources (money gifts):	
(i) Cash gift from a friend, by cheque	50,000
(ii) Cash gift from nephew, not covered by the definition of relative	1,00,000
(iii) Gift of diamond ring — non-monetary gift not taxable	—
(iv) Cash gifts on the occasion of marriage are not chargeable even if such gifts are made by unrelated persons	—
(v) Cash gift made by wife's sister, a relative, not taxable	—
(vi) Cash gift by a friend of father-in-law, unrelated person	1,51,000
(vii) Cash gift made by great-grand father, a relative	—
(viii) Cash gift received under Will in contemplation of death of a friend	—
(ix) Cash gift made by a business friend on his birthday	51,000
(x) Cash gifts, made by three friends, of ₹ 25,000 each	75,000
Total income	6,02,000

Question 12. Mr Ayan Goel receives the following gifts of money:

S. No.	Date of gift	Donor	Form of gift	Amount of gifts	Remarks
1.	31.3.2011	Friend	Cheque	25,000	Cheque is encashed on 03.04.2011
2.	01.05.2011	Brother	Bank draft	50,000	
3.	30.07.2011	Non-resident friend	Cheque	30,000	
4.	01.10.2011	Brother-in-law	Cash	10,000	
5.	15.11.2011	Great-grandfather-in-law	Cash	40,000	On the occasion of the marriage Maturity date 31.03.2011
6.	05.12.2011	Cousin brother	Cash	21,000	
7.	01.01.2012	Neighbour	NSC-VIII Issue	10,000	
8.	31.03.2012	Friend	Cash	10,000	

Determine the chargeability of the aforesaid gifts. Would it make any difference if the amount of gift made on 31.03.2012 is ₹ 10,001.

Solution : Computation of taxable gifts for the AY 2012-2013.

	Particulars	Case – I ₹	Case – II ₹
1.	Gift of cheque dated 31.03.2011 from a friend but encashed on 03.04.2011 is not taxable since it does not exceed ₹ 25,000. Chargeability is governed by the date of receipt and not by date of encashment.	—	—
2.	Gift from brother is exempt	—	—
3.	Gift from friend	30,000	30,000
4.	Gift from brother-in-law—Exempt	—	—
5.	Gift from great grandfather-in-law: Exempt	—	—
6.	Gift on the occasion of the marriage	—	—
7.	Gift from neighbour	10,000	10,000
8.	Gift from friend	10,000	10,000
		<u>50,000</u>	<u>50,000</u>
	Taxable gift	Exempt	50,001



STUDY NOTE - 9

CLUBBING OF INCOME

This Study Note includes

- Clubbing provisions for inclusion in assessee's income, income of some other person

9.1 CLUBBING OF INCOME

Certain provisions are included in the act as anti tax avoidance measures. Provisions for inclusion in assessee's income, income of some other person, who is not at arm's length, are a kind of such provisions. Such provisions arrest tax leakage likely to result from certain transactions with relatives or diversion of title without losing control over the same, etc.

ENCOMPASS OF CLUBBING PROVISIONS

1	Clubbing of income where control over assets or income is retained while title is transferred	Sections 60, 61, 64(1)(iv),(vi),(vii),(viii)
2	Clubbing of income of relatives under certain circumstances.	Sections 64(ii)
3	Clubbing of income of minor child	Section 64(1A)

TRANSFER OF ASSETS [Sec. 60]

Where any person transfers income without transferring the ownership of the asset, such income is taxable in the hands of the transferor. Such transfer may be revocable or irrevocable. The provision applies irrespective of the time when the transfer has been made i.e. it may be before or after the commencement of the Income-tax Act.

REVOCABLE TRANSFER OF ASSETS [Sec. 61]

Any income arising to any person by virtue of revocable transfer of assets is chargeable to tax as the income of transferor. For this purpose, transfer may include any settlement or agreement.

The transfer is said to be revocable if it contains any provision for the re-transfer of the whole or any part of the income or assets to the transferor a right to reassume power over the whole or any part of the income or assets.

If any settlement contains a clause for forfeiture of rights of beneficiaries under certain circumstances, the settlement will be regarded as revocable – CIT v. Bhuvaneshwar Kuer 53 ITR 195 (SC).

This section is, however, not applicable in the following cases-

- Where the income arises to any person by virtue of a transfer by any of the trust, which is not revocable, during the lifetime of the beneficiary and, in case of any transfer, which is not revocable, during lifetime of the transferee.
- Where the income arises to any person by virtue of a transfer made before 1.4.1986, which is not revocable for a period of six years or more. However, income will be chargeable to tax as the income of the transferor as and when the power to revoke the transfer comes into play.

IRREVOCABLE TRANSFER OF ASSETS FOR SPECIFIED PERIOD [Sec.62]

- The provisions of section 61 shall not apply to any income arising to any person by virtue of a transfer—
 - by way of trust which is not revocable during the lifetime of the beneficiary, and, in the case of any other transfer, which is not revocable during the lifetime of the transferee ; or

- (ii) made before the 1st day of April, 1961, which is not revocable for a period exceeding six years :

Provided that the transferor derives no direct or indirect benefit from such income in either case.

- (2) Notwithstanding anything contained in sub-section (1), all income arising to any person by virtue of any such transfer shall be chargeable to income-tax as the income of the transferor as and when the power to revoke the transfer arises, and shall then be included in his total income.

TRANSFER AND REVOCABLE TRANSFER DEFINED [Sec.63]

For the purposes of sections 60, 61 and 62 and of this section,—

- (a) a transfer shall be deemed to be revocable if—
- (i) it contains any provision for the re-transfer directly or indirectly of the whole or any part of the income or assets to the transferor, or
 - (ii) it, in any way, gives the transferor a right to re-assume power directly or indirectly over the whole or any part of the income or assets ;
- (b) “transfer” includes any settlement, trust, covenant, agreement or arrangement

REMUNERATION OF SPOUSE [Sec. 64(1)(ii)]

An individual assessee is chargeable to tax in respect of any remuneration received by the spouse from a concern in which the individual has substantial interest. However, remuneration which is solely attributable to technical or professional knowledge and experience of the spouse, will not be clubbed. Where both the spouses have a substantial interest in the concern and both are in receipt of the remuneration for such concern, such remuneration will be included in the total income of the husband or wife whose total income excluding such remuneration is greater.

The individual is deemed to have substantial interest, if the beneficiary holds equity share carrying not less than 20% voting power in the case of a company or is entitled to not less than 20% of the profits, in any other concern, not being a company at time during the Previous Year.

INCOME FROM ASSETS TO SPOUSE [Sec. 64(1)(iv)]

Where an asset (other than House Property) is transferred by an individual to his or her spouse directly or indirectly otherwise than for adequate consideration or in connection with an agreement to live apart any income from such asset will be deemed to be the income of transferor.

However, this section is not applicable in the following cases—

- (a) if assets are transferred before marriage.
- (b) if assets are transferred for adequate consideration.
- (c) if assets are transferred in connection with an agreement to live apart.
- (d) if on the date of accrual of income, the transferee is not spouse of the transferor.
- (e) if property is transferred by the Karta of HUF, gifting co-parcenary property to his wife.
- (f) the property is acquired by the spouse out of the pin money (i.e., an allowance given to the wife by her husband for her dress and usual household expenses).

INCOME FROM ASSETS TRANSFERRED TO SON'S WIFE OR MINOR CHILD [Sec. 64(1)(vi)]

If an individual directly or indirectly transfers the assets after 1.6.73 without adequate consideration to son's wife or son's minor child (including son's minor step child or son's minor adopted child), income arising from such assets will be included in the total income of the transferor from the Assessment Year 1976-77 onwards.

INCOME FROM ASSETS TRANSFERRED TO A PERSON FOR THE BENEFIT OF SPOUSE OR MINOR CHILD [Sec. 64(1)(vii)]

Where an asset is transferred by individual, directly or indirectly, without adequate consideration to a person or persons for the immediate or deferred benefits of his or her spouse, income arising from the transferred assets will be included in the total income of the transferor to the extent of such benefit. If no income is accrued out of the property transferred by an individual, then nothing will be included in the income of the individual.

**INCOME FROM ASSET TRANSFERRED TO A PERSON FOR THE BENEFIT OF SON'S WIFE [Sec. 64 (1)(viii)]**

Where an asset is transferred by an individual, directly or indirectly, or after 1.6.73 without adequate consideration to a person or an association of persons for the immediate or deferred benefits of son's wife, income arising directly or indirectly from transferred asset will be included in the total income of the transferor to the extent of such benefit with effect from the Assessment Year 1985-86.

INCOME OF MINOR CHILD [Sec. 64(1A)]

In computing the total income of any individual, there shall be included all such income as arises or accrues to his minor child. However, income of the following types will not be included in the total income of the individual where income arises or accrues to the minor child on account of any—

- (a) manual work done by him; or
- (b) activity involving application of his skill, talent or specialised knowledge and experience.

Person in whose hands to be clubbed :

- (i) 1st year : that parent whose income is higher. Subsequent years; the same parent – unless the AO is satisfied that it should be clubbed with the other parent.
- (ii) where marriage does not subsist, in the hands of the custodian parent.

However, a deduction — Upto ₹. 1,500 per minor [Sec. 10(32)] shall be allowed against such income which is clubbed in the hands of the parent.

CONVERSION OF SELF-ACQUIRED PROPERTY INTO JOINT FAMILY AND SUBSEQUENT PARTITION [Sec. 64(2)]

Where a member of a HUF has converted his self-acquired property into joint family property after 21.12.1969, income arising from the converted property will be dealt with as follows :-

- (i) For the Assessment Year 1976-77 onwards, the entire income from the converted property is taxable as the income of the transferor.
- (ii) If the converted property is subsequently partitioned amongst the members of the family, the income derived from such converted property, as is receivable by the spouse and minor child of the transferor will be taxable in his hands.

INCOME FROM THE ACCRETION TO ASSETS

In the above mentioned cases the income arising to the transferee from the property transferred, is taxable in the hands of the transferor. However, income arising to the transferee from such property is not includible in the total income of the transferor. Thus, if Mr. A transfers ₹. 60,000 to his wife without any adequate consideration and Mrs. A deposits the money in a bank, the interest received from the bank on such deposits is taxable in the hands of Mr. A. If however, Mrs. A purchases shares in a company from the accumulated interest, the dividend received by Mrs. A, will be taxable in her hands and will not be clubbed with the income of Mr. A.

CLUBBING OF NEGATIVE INCOME [EXPLANATION TO Sec. 64]

The income of a specified person is liable to be included in the total income of the individual in the circumstances mentioned earlier. For the purposes of including income of the specified person in the income of the individual, the word "income" includes a loss.

RECOVERY OF TAX U/S. 60 TO 64 [Sec. 65]

As per incomes belonging to ss. 60 to 64 to other persons are included in the total income of the assessee in such cases, by virtue of sec. 65, the actual recipient of income is liable, on the service of notice of demand, to pay the tax assessed in respect of income included in the income of other person (where the Income Tax Officer so desires).

PROBLEMS ON CLUBBING OF INCOME

1. Mrs.G holds 7% equity shares in B Ltd., where her married sister, Mrs. N also holds 14% equity shares. Mr.G is employed with C Ltd., without holding technical professional qualification. The particulars of their income for the previous year 2011-2012 are given as follows:

	Income of Mr G ₹	Income of Mrs G ₹
(i) Gross salary from B Ltd.	1,02,000	—
(ii) Dividend from B Ltd.	—	6,000
(iii) Income from house property	90,000	—

Solution : **Computation of Total income of Mr. G & Mrs. G for the A.Y. 2012-2013**

Particulars	Mr. G ₹	Mrs. G ₹
Gross salary		1,02,000
Taxable salary to be included in the total income of Mrs G [Sec. 64(1)(ii)]		
Add: Income from house property	90,000	
Add: Income from other sources : Dividends to Mrs G, but exempt under Sec. 10(34)	Nil	
Total Income	90,000	1,02,000

Note:

1. In the instant case, Mrs G along with his sister, holds substantial interest in B Ltd., Mr. G does not hold professional qualification. Accordingly, remuneration of Mr.G has been included in the total income of Mrs. G.
2. If the requisite conditions of clubbing are satisfied, clubbing provision will apply even if their application results into lower incidence of tax.

2. Mrs. C, a law graduate, is legal advisor of L Ltd. She gets salary of ₹ 1,80,000. Mr. C is holding 20% shares in L Ltd. His income from business, during the previous year 2011-2012 is ₹ 4,00,000. Compute their total income.

Solution : **Computation of Total income of Mr. C & Mrs. C for the A.Y. 2012-2013**

Particulars	Mr. C ₹	Mrs. C ₹
1. Gross salary		1,80,000
2. Business profits	4,00,000	—
Total income	4,00,000	1,80,000

Note: Since Mrs. C holds professional qualification, salary income is assessable in her hands.

3. Mr B holds 5% shares in A Ltd., where his brother and nephew hold 11% and 6% shares, respectively. Mrs B gets commission of ₹ 1,00,000 from A Ltd. for canvassing orders. She holds no technical/professional qualification. Mr B earns income of ₹ 5,00,000 from sugar business.

Compute their total income for the assessment year 2012-13.

Solution :
Computation of Total Income for the AY 2012-13

Particulars of income	Mr. B ₹	Mrs. B ₹
Income from sugar business Commission for canvassing orders from Z Ltd.: Income from other sources	2,00,000	90,000
Total Income	2,00,000	90,000

Note: In the instant case, Mr B holds 7% and his brother holds only 12% shares in A Ltd. The total of their shareholding is less than 20%. They have no substantial interest.

Therefore, commission income is assessable as income of Mrs B.

4. The shareholding of Mr K and Mrs K in S Ltd, is given as follows:

(i) Shareholding of K	7%
(ii) Shareholding of Mrs K	9%
(iii) Shareholding of M, brother of K	8%
(iv) Shareholding of F, father of Mrs K	5%

Mr K and Mrs K are employed with S Ltd. None of them hold technical qualification. Mr K gets salary @ ₹ 10,000 p.m and Mrs K gets @ ₹ 12,000 p.m.

Income from other sources:	₹
Mr K	80,000
Mrs K	1,00,000

Compute total income for the assessment year 2012-2013

Solution :
Computation of Total Income for the AY 2012-13

Particulars	Mr.K	Mrs.K
1. Gross Salary	<u>1,20,000</u>	1,44,000
Salary income of Mr.K to be included in the total income of Mrs.K as her income from other sources is greater and both of them have substantial interest alongwith their relative in s Ltd.		1,20,000
2. Income from other sources	<u>80,000</u>	<u>1,00,000</u>
Total Income	<u>80,000</u>	<u>3,64,000</u>

5. Mr A gifts ₹ 4,00,000 to Mrs A 1st February 2012. Mrs A starts crockery business and invests ₹ 1,00,000 from her account also. She earns profit of ₹ 60,000 during the period ending on 31 March 2012. How would you tax the business profits?

Answer: Proportionate profits, in proportion the gifted amount from the spouse on the first day of the previous year bears to the total investment in the business on the first day of the previous year, will be taxable in the income of the transferor spouse:

As Mrs A has started the new business, the first previous year will begin on the date of setting up and will end on 31 March, immediately following. Thus, the first previous year will consist a period of 2 months from 1 February 2011, to 31 March 2012. Therefore, proportionate profit of ₹ 50,000, computed as below, will be included in the income of Mr. A:

$$\frac{4,00,000}{5,00,000} \times 60,000 = 48,000$$

6. Mr A gifts ₹ 3,00,000 to Mrs A on 1st February 2012. Mrs A invests the same in the existing crockery business where she has already invested ₹ 5,00,000. Mrs. A earns ₹ 3,00,000 from the business during the year 2011-2012 ending on 31 March 2012. How would you assess the profits?

Answer : The previous year of the existing business is April to March. On the first day of the previous year (i.e. 1 April 2011), total investment has come from Mrs A account. As the proportion of the gifted amount from spouse on 1 April 2011 to the total investment in business on the same day is **NIL**, the whole of the profits of ₹ 3,00,000 for the year 2011-2012 will be included in the total income of Mrs A.

From the previous year 2011-2012, 60% [= 3,00,000/5,00,000 × 100] of the business profits will be included in the total income of Mr A.

7. Mrs Z is the owner of the business units A and B. A unit has been started with capital contribution from Mr Z and B unit has been started out of capital contribution from Mrs.Z. The particulars of their income for the previous year 2011-2012 are as follows:

Particulars	Mrs Z	Mr Z
(i) Income from A unit	—	(-) 6,00,000
(ii) Income from B unit	4,00,000	—
(iii) Income from house property		2,50,000

How would you assess them for the assessment year 2012-2013?

Answer :

- Mrs Z is assessable on the profits from B unit. She cannot set-off the loss from A unit against the profits of B unit. Thus, she would be assessed on ₹ 4,00,000.
- The loss from A unit will be included in the total income of Mr Z in view of Sec. 64(1)(iv). "Income" includes "loss" also. Mr Z is entitled to set-off business loss of A's unit against income from house property. Thus, loss of ₹ 3,50,000 would be carried forward but could be set-off only against business profits.

8. Mr Goutam, out of his own funds, had taken a FDR for ₹ 1,00,000 bearing interest @ 10% p.a. payable half-yearly in the name of his wife Latika. The interest earned for the year 2011-2012 of ₹ 10,000, was invested by Mrs Latika in the business of packed spices which resulted in a net profit of ₹ 55,000 for the year ended 31st March 2012. How shall the interest on FDR and income from business be taxed for the Assessment year 2012-2013?

Answer: Where an individual transfers an asset (excluding house property), directly or indirectly to his/her spouse, otherwise than for adequate consideration, or in connection with an agreement to live apart, income from such asset is included in the total income of such individual [Sec. 64(1)(iv)].

Accordingly, interest on FDR, accruing to wife, is included in the total income of her husband. However, business profits cannot be clubbed with total income of husband. Clubbing applies only to the income from assets transferred without adequate consideration. It does not apply to the income from accretion of the transferred assets. Hence, business profit is taxable as the income of wife.

9. Sawant is a fashion designer having lucrative business. His wife is a model. Sawant pays her a monthly salary of ₹ 20,000. The Assessing Officer while admitting that the salary is an admissible deduction, in computing the total income of Sawant had applied the provisions of Sec. 64(1) and had clubbed the income (salary) of his wife in Sawant's hands.

Discuss the correctness of the action of the Assessing Officer.

Answer: Where an individual has got substantial interest in a concern and his spouse derives any income from such concern by way of salary, commission, fees or by any other mode, such income is clubbed with the total income of such individual [Sec. 64(1)(ii)].

However, clubbing provision does not apply if the earning spouse holds technical or professional qualification and the income is solely attributable to the application of such knowledge and experience.

Salary earned by wife as model from the concern where her husband holds substantial interest is assessable as her income.

10. Discuss whether the loss could be set-off in the following case:

Smt. Vatika carried on business with the gifted funds of her husband Mr.Dabuu. For the previous year ending 31.3.2011, Vatika incurred loss of ₹ 5 lakh which loss Dabuu wants to set-off from his taxable income.

Answer: Funds for business were gifted by husband to wife. Accordingly, income from business should be clubbed with the income of husband [Sec. 64(1)(iv)].

"Income" includes "loss" also. Hence, husband is entitled to set-off the business loss of wife against his taxable income.



STUDY NOTE - 10

SET OFF OR CARRY FORWARD AND SET OFF OF LOSSES

This Study Note includes

- Various Provisions under the Income Tax Act relating to set off or carry forward and set off of losses

INTRODUCTION

If income is one side of the coin, loss is the other side. When a person earns income, he pays tax. However, when he sustains loss, law affords him to have benefit in the form of reducing the said loss from income earned during the subsequent years. Thus, tax liability is reduced at a later date, if loss is sustained. Certain provisions govern the process of carry forward and set off of loss.

This will be discussed on :

1. Set off of Loss in the Same Year
2. Carry forward and Set off of Loss in Subsequent Years
 - i) Basic Conditions for carry forward of loss.
 - ii) Conditions applicable to each Head of Income

As stated in section 14 of the Act computation of total income is made under certain heads viz. (i) Salaries (ii) Income from House Property (iii) Profits and gains of Business or Profession (iv) Capital gains and (v) Income from other sources.

In case computation results in to a positive figure, it is income. Likewise, if the computation results into a negative figure, it is 'Loss'. Therefore, there cannot be loss from the head 'Salary'. Loss can occasion from all the remaining heads.

10.1 SET OFF OF LOSS IN THE SAME YEAR

For the purpose of computing total income and charging tax thereon, income from various sources is classified under the following heads :

- A. Salaries
- B. House Property
- C. Profits and gains of Business or Profession
- D. Capital gains
- E. Other sources

These five heads of income are mutually exclusive. If any income falls under one head, it cannot be considered under any other head. Income under each head has to be computed as per provisions under that head. Then, subject to provisions of Set off of Losses (Sec. 70 to Sec. 80) between the heads of income, the income under various heads has to be added to arrive at a gross total income. From this gross total income, deductions under chapter VIA are to be allowed to arrive at the total income.

In this part, the provisions relating to set off, carry forward and set off of losses are categorised as under :-

SECTION 70

Where the net result for any Assessment Year in respect of any source falling under any head of income is a loss, the assessee shall be entitled to have the amount of such loss set off against his income from any other source under the same head.

- (1) Save as otherwise provided in this Act, where the net result for any assessment year in respect of any source falling under any head of income, other than "Capital gains", is a loss, the assessee shall be entitled to have the amount of such loss set off against his income from any other source under the same head.
- (2) Where the result of the computation made for any assessment year under sections 48 to 55 in respect of any short-term capital asset is a loss, the assessee shall be entitled to have the amount of such loss set off against the income, if any, as arrived at under a similar computation made for the assessment year in respect of any other capital asset.
- (3) Where the result of the computation made for any assessment year under sections 48 to 55 in respect of any capital asset (other than a short-term capital asset) is a loss, the assessee shall be entitled to have the amount of such loss set off against the income, if any, as arrived at under a similar computation made for the assessment year in respect of any other capital asset not being a short-term capital asset.]

SECTION 71

Where the net result of the computation under any head of income in respect of any Assessment Year is a loss, the assessee shall be entitled to have such amount of loss set off against his income assessable for that Assessment Year under any other head of income.

Exceptions to provisions of sections 70 and 71 are as follows :

- (a) **Loss from speculation business:** "Speculation transaction" means a transaction in which a contract for the purchase or sale of any commodity including stocks and shares is periodically or ultimately settled otherwise than by actual delivery or transfer of the commodity or scripts. [Sec. 43(5)] Loss from speculative transaction, if it is in the nature of business, can be set off only against income of another speculative business.
- (b) **Loss under the head long term capital gains** arising from transfer of long-term capital assets will be allowed to be set off only against long term capital gains.

Note:

1. Loss can be set off against deemed income.
2. Inter head adjustment is made only when the net income computed under a head is a loss.
3. The scheme of inter source and inter head adjustment is mandatory.
- (c) **Loss from owning and maintaining race horses** can be set off only against income of that activity.
- (d) No expenditure or allowance is allowed from wining from lotteries, crossword puzzles, card games etc. similarly, no loss from any lottery, card games, races, etc. is allowed to be set off from the income of such sources. [Sec. 58(4)]
- (e) loss incurred by an assessee from a source, income from which is exempt cannot be set off against income from a taxable source.

10.2 CARRY FORWARD AND SET OFF OF LOSS IN SUBSEQUENT YEARS BASIC CONDITIONS FOR CARRY FORWARD OF LOSS

SECTION 80: LOSS RETURNS.

In order to carry forward loss under section 72, 73, 74 and 74A. The due date is prescribed in section 139(1). No loss which has not been determined in pursuance of a return filed within the date in accordance with the provisions of section 139(3) shall be carried forward under the provisions of section.

The condition for filing of return in accordance with the provisions of sec. 139(3) shall not apply to loss from House Property carried forward u/s. 71B and unabsorbed depreciation u/s. 32(2).

Brought forward loss of earlier assessment Year in accordance with Ss. 72, 73, 74, 74A can be set off against the income of that Assessment Year and can be carried forward further, even if the return is not filed within the due date specified in section 139(1) of the Act.



CBDT has issued circular vide No. 8 of 2001 dated 16.5.2001 clarifying that the power has been delegated to Commissioner to condone delay in filing return and carry forward losses in cases where the claim for loss does not exceed ₹ 10,000 for each Assessment Year and to Chief Commissioner/Director General upto ₹ 1 lakh and beyond such limit CBDT will exercise the power.

CONDITIONS APPLICABLE TO EACH HEAD

71B. Carry forward and set off of loss from house property

Where for any assessment year the net result of computation under the head “Income from house property” is a loss to the assessee and such loss cannot be or is not wholly set off against income from any other head of income in accordance with the provisions of section 71 so much of the loss as has not been so set-off or where he has no income under any other head, the whole loss shall, subject to the other provisions of this Chapter, be carried forward to the following assessment year and—

- (i) be set off against the income from house property assessable for that assessment year; and
- (ii) the loss, if any, which has not been set off wholly, the amount of loss not so set off, shall be carried forward to the following assessment year, not being more than eight assessment years immediately succeeding the assessment year for which the loss was first computed.

Sec 72AA: Carry forward and set –off accumulated loss in scheme of amalgamation of banking company

Where there has been an amalgamation of

- (a) a company owning an industrial undertaking or a ship or a hotel with another company; or
- (b) a banking company referred to in clause (c) of section 5 of the Banking Regulation Act, 1949 (10 of 1949) with a specified bank; or
- (c) one or more public sector company or companies engaged in the business of operation of aircraft with one or more public sector company or companies engaged in similar business.

accumulated loss and the unabsorbed depreciation of such company shall be deemed to be the loss of such banking institution for the previous year in which the scheme of amalgamation was brought into force.

Provision relating to carry forward and set- off of accumulated loss and unabsorbed depreciation allowance in a scheme of amalgamation of banking company in certain cases [Section 72 AA]

Notwithstanding anything contained in section 72(2)(1B)(i) to (iii) where there has been an amalgamation of a banking company with any other banking institution under a scheme sanctioned and brought into force by the Central Government under sec 45(7) of Banking Regulation Act, 1949 the accumulated loss and the unabsorbed depreciation of such banking company shall be deemed to be the loss or, as the case may be, allowance for depreciation of such banking institution for the previous year in which the scheme of amalgamation was brought into force and other provision of this Act relating to set- off and carry forward of loss and allowance for depreciation shall apply accordingly.

For the purposes of this section :

- (i) “Accumulated loss” means so much of the loss of the amalgamating banking company, under the head “Profits and gains business” (not being a loss sustained in a speculation business) which such amalgamating banking company, would have been entitled to carry forward and set-off under the provision of section 72 if the amalgamation had not taken place;
- (ii) “banking company” shall have the same meaning assigned to it in sub-section (15) of section 45(15) of the Banking Regulation Act, 1949.
- (iii) “banking institution” shall have the same meaning assigned to it in sub-section (15) of sec 45(15) of the Banking Regulation Act, 1949.
- (iv) “unabsorbed depreciation” means so much of the allowance for depreciation of the amalgamating banking company which remains to be allowed and which would have been allowed to such banking company if amalgamation had not taken place.

Provisions relating to carry forward and set off of accumulated loss and unabsorbed depreciation allowance in business reorganisation of co-operative banks [Sec. 72AB]

- (1) The assessee, being a successor co-operative bank, shall, in a case where the amalgamation has taken place during the previous year, be allowed to set off the accumulated loss and the unabsorbed depreciation, if any, of the predecessor co-operative bank as if the amalgamation had not taken place, and all the other provisions of this Act relating to set off and carry forward of loss and allowance for depreciation shall apply accordingly.**
- (2) The provisions of this section shall apply if—**
 - (a) the predecessor co-operative bank—**
 - (i) has been engaged in the business of banking for three or more years; and
 - (ii) has held at least three-fourths of the book value of fixed assets as on the date of the business reorganisation, continuously for two years prior to the date of business reorganisation;
 - (b) the successor co-operative bank—**
 - (i) holds at least three-fourths of the book value of fixed assets of the predecessor co-operative bank acquired through business reorganisation, continuously for a minimum period of five years immediately succeeding the date of business reorganisation;
 - (ii) continues the business of the predecessor co-operative bank for a minimum period of five years from the date of business reorganisation; and
 - (iii) fulfils such other conditions as may be prescribed to ensure the revival of the business of the predecessor co-operative bank or to ensure that the business reorganisation is for genuine business purpose.
- (3) The amount of set-off of the accumulated loss and unabsorbed depreciation, if any, allowable to the assessee being a resulting co-operative bank shall be,—**
 - (i) the accumulated loss or unabsorbed depreciation of the demerged co-operative bank if the whole of the amount of such loss or unabsorbed depreciation is directly relatable to the undertakings transferred to the resulting co-operative bank; or
 - (ii) the amount which bears the same proportion to the accumulated loss or unabsorbed depreciation of the demerged co-operative bank as the assets of the undertaking transferred to the resulting co-operative bank bears to the assets of the demerged co-operative bank if such accumulated loss or unabsorbed depreciation is not directly relatable to the undertakings transferred to the resulting co-operative bank.
- (4) The Central Government may, for the purposes of this section, by notification in the Official Gazette, specify such other conditions as it considers necessary, other than those prescribed under sub-clause (iii) of clause (b) of sub-section (2), to ensure that the business reorganisation is for genuine business purposes.**
- (5) The period commencing from the beginning of the previous year and ending on the date immediately preceding the date of business reorganisation, and the period commencing from the date of such business reorganisation and ending with the previous year shall be deemed to be two different previous years for the purposes of set off and carry forward of loss and allowance for depreciation.**
- (6) In a case where the conditions specified in sub-section (2) or notified under sub-section (4) are not complied with, the set off of accumulated loss or unabsorbed depreciation allowed in any previous year to the successor co-operative bank shall be deemed to be the income of the successor co-operative bank chargeable to tax for the year in which the conditions are not complied with.**

Insertion of section 73A for set off loss of the specified business : (w.e.f A.Y. 2010-11)

With reference to newly inserted Section 35AD (w.e.f A.Y. 2010-11). Any loss computed in respect of the specified business shall not be set off except against profits and gains, if any, of any other specified business. To the extent business in the following assessment year and so on.

Section	Losses
72	Carried forward and set-off of business losses other than speculative business.
73	Losses in speculation business.
74	Losses under the head Capital Gains.
74A	Losses from owning and maintaining race Horses.

Sec	Nature of loss	Details of set off	Conditions / Exceptions
72	Brought forward unabsorbed business loss other than Speculation loss	Set off only against income under the head profits and gains of business or profession.	1. Carry forward and set off is permissible for 8 assessment years immediately succeeding the assessment year for which the loss was computed. 2. Loss can be carried forward only if the return is filed u/s 139(1) and it is determined and communicated u/s 157.
32(2)	Brought forward unabsorbed depreciation	Set off against any head of income	Unabsorbed depreciation loss can be carried forward for any number of years until it is fully set off.
73	Brought forward unabsorbed Speculation business loss	Set off only against income under Speculation business	1. Carry forward and set off is permissible for 4 assessment years immediately succeeding the assessment year for which the loss was computed. 2. Loss can be carried forward only if the return is filed u/s 139(1) and it is determined & communicated u/s 157.
74	Brought forward unabsorbed loss under the head Capital Gains.	Set off only against income under the head Capital Gain.	1. Carry forward and set off is permissible for 8 assessment years immediately succeeding the assessment year for which the loss was computed. 2. STCL can be set off against any Capital Gain. However, LTCL can be set off only against LTCG. 3. Loss can be carried forward only if the return is filed u/s 139(1) and it is determined & communicated u/s 157.
74A	Brought forward unabsorbed loss from activity of owning & maintaining race horses	Set off only against income from owning and maintaining race horses	1. Carry forward and set off is permissible for 4 assessment years immediately succeeding the assessment year for which the loss was computed. 2. Loss can be carried forward only if the return is filed u/s 139(1) and it is determined & communicated u/s 157.

SPECIAL PROVISIONS

Section 78(1):

Where a change has occurred in the constitution of the firm, the firm shall not be entitled to carry forward and set off so much of the loss proportionate to the share of a retired or deceased partner remaining unabsorbed shall not be allowed to be carried forward by the firm. These restriction shall not apply to unabsorbed depreciation.

Change in constitution of the firm takes place :-

- If one or more of the partners cease to be partners or one or more new partners are admitted, in such circumstances that one or more of the persons who were partners of the firm before the change continue as partner or partners after the change (provided the firm is not dissolved on the death of any of its partners).



- (ii) Where all the partners continue with a change in their respective shares or in the shares or in the shares of some of them.

Section 78(2) :

Where any person carrying on any Business or Profession has been succeeded in such capacity by another person otherwise than by inheritance, then the successor cannot have the loss of predecessor carried forward and set off against his income.

Section 79 :

Losses (other than unabsorbed depreciation) in case of closely held company

In case of a company in which public are not substantially interested (defined in sec. 2(18) of the Act), the unabsorbed business loss relating to any Assessment Year can be carried forward and set off against the income in a subsequent Assessment Year only (if the shares of the company carrying not less than 51% of the voting power were beneficially held by the same persons) both on the last day of the Previous Year(s) in which the loss, claimed to be set off and on the last day of the Previous Year in which loss was incurred.

Exceptions

The provisions stated supra shall not apply if the change in the voting power takes place due to the following reasons :

- (a) the death of a shareholder; or
- (b) transfer of shares by way of gifts to any relative of the shareholder making such gift.
- (c) W.e.f. AY 2000-01, this section shall not apply to any change in the shareholding of an Indian company which is subsidiary of a foreign company arising as a result of amalgamation or demerger of a foreign company subject to the condition that 51% of the shareholders of the amalgamating or demerged foreign company continue to remain the shareholders of the amalgamated or the resulting foreign company.

Notes : Unabsorbed business losses can be carried forward and set off against profits from any business from A.Y. 2000-01. There is no need to continue the same business in which the loss was incurred.

Depreciation can be carried forward and set off against the profits from any business in the succeeding assessment year up to A.Y. 2001-02. The business in which the loss was incurred need not be continued in that year.

The effect of depreciation, business loss and investment allowance should be given in the following order:

- Current year's Depreciation
- Unabsorbed Business loss
- Unabsorbed Depreciation
- Unabsorbed Investment Allowance.

A return of loss is required to be furnished for determining the carry forward of such losses, by the due date prescribed for different assesses under section 139(1) of the Act. (Sec. 80).



PROBLEMS ON SET-OFF AND CARRY FORWARD OF LOSSES

1. Following are the particulars of the income of Mr. Srikant for the previous year 2011-2012

	₹
1. Income from house property	
(a) Property R	(+) 12,000
(b) Property J	(-) 20,000
2. Profits and gains from business:	
(A) Non-speculation:	
(i) Business X	40,000
(ii) Business Y	(-) 50,000
(B) Speculation:	
(i) Silver	40,000
(ii) Bullion	(-) 10,000
3. Capital gains:	
(i) Long-term capital gains	(+) 30,000
(ii) Short-term loss	(-) 10,000
4. Income from other sources:	
(i) Card games-loss	10,000
(ii) From the activity of owing and maintaining race horses:	
(a) Loss at Mumbai	(-) 50,000
(b) Profit at Kolkata	(+) 40,000
(iii) Dividend from Indian companies	10,000
(iv) Income by letting out plant and machinery	1,11,000
The following losses have been carried forward:	
(i) Long-term capital loss from the assessment year 2007-2008:	18,000
(ii) Loss from silver speculation from the assessment year 2007-2008 and which was discontinued in the assessment year 2008-2009	25,000

Compute the gross total income for the assessment year 2012-2013.

Solution : **Computation of Gross Total Income for the Assessment Year 2012-2013**

Particulars	₹	₹
1. Income from house property (+ 12,000 - 20,000)		(-) 8,000
2. Profits from speculation:		
(i) Profit from Silver Business	40,000	
Less: Current year loss from bullion	(-) 10,000	
	30,000	
Less: Carried forward silver speculative loss	(-) 25,000	
Surplus from Speculation	5,000	
(ii) Add: Business profit from X business	40,000	
(iii) Less: Business loss from Y business	(-) 50,000	(-) 5,000

Unabsorbed business loss may be set-off against the income of any other head except 'salaries' and 'winnings from lottery, card games, crossword puzzle, betting on race horses', etc.

3. Capital gains:		
Long-term capital gains	30,000	
Less : Short-term capital loss	(-) 10,000	
Long-term capital gain	<u>20,000</u>	20,000
4. Income from other sources:		
(i) Income by letting out plant and machinery		1,11,000
(ii) Card game-loss of ₹ 10,000		
Neither it can be set-off nor it can be carried forward		
(iii) Profit from race horses at Kolkata	(+) 40,000	
Less : Loss from race horses at Mumbai	(-) 50,000	
Less : to be carried forward for next four assessment year	(-) 10,000	
(iv) Dividend from Indian companies: Exempt under Sec. 10(34)		Nil
Aggregated income after setting-off current year losses from house property, profit and business against income from other sources:		<u>1,18,000</u>
Less : Carried forward long-term capital loss, from the assessment year 2007-2008 to be set-off against long-term capital gains		18,000
Gross total income or total income as there is no deduction available from GTI		<u>1,00,000</u>

2. Mr. Dey furnishes the following particulars of his income for the previous year 2011-2012:

Particulars	₹
Unit "A": Business loss	(-) 4,00,000
Unabsorbed depreciation	(-) 2,00,000
Unit "B": Business profit	10,00,000
Income from house property	2,00,000
Carried forward losses and allowance;	
Unit "C" business was discontinued on 31-12-2005	
Apart from the abovementioned, the following unabsorbed:	
1. Business loss	(-) 3,00,000
2. Depreciation	(-) 2,00,000
Unit "D" business was discontinued on 1-3-2008 leaving the following unabsorbed:	
1. Business loss	(-) 3,00,000
2. Depreciation	(-) 1,00,000

Compute his total income for the assessment year 2012-13.



Solution :

Computation of total income for the AY 2012-2013

Particulars	₹	₹
Income from house property		2,00,000
Business - profession		
Profit of B-business	(+) 10,00,000	
Less: Business loss of A - business	(-) 4,00,000	
Depreciation of A-business	(-) 2,00,000	
	(+) 4,00,000	4,00,000
Aggregated income		6,00,000
Less: Carried forward business loss:		
(i) Loss of C Business to be set-off against business profits	(-) 3,00,000	
(ii) Loss of D business	(-) 3,00,000	
	6,00,000	(-) 6,00,000
Total income		Nil

Note : Where business loss and depreciation both are being carried forward, business loss has got priority, over depreciation. Unabsorbed depreciation is carried forward without time-limit.

3. XYZ & Co., a partnership firm, submits the following particulars of its income and carry forward losses for the previous year 2011-2012:

Particulars	Betting on race horses made lawfully (₹)	Betting on race horses made illegally (₹)
1. Gross prize on race horses	15,00,000	5,00,000
2. Expenses incurred:		
(i) Horses purchased during the year	6,00,000	75,000
(ii) Medical expenses	1,00,000	20,000
(iii) Animal trainer fees	50,000	15,000
(iv) Fodder expenses	2,60,000	50,000
(v) Stable-rent/insurance	1,20,000	36,000
(vi) Depreciation in the value of horses	4,60,000	1,50,000
(vii) Staff salaries	1,00,000	40,000
3. Losses brought forward from the assessment year 2010-2011	6,00,000	2,00,000

Solution :

Computation of total income for the Assessment Year 2012-13

Particulars	Betting on race horses made lawfully (₹)	Betting on race horses made illegally (₹)
Gross prize		
Less: Expenses incurred:	15,00,000	15,00,000
(i) Horses purchased—not allowed	—	—
(ii) Medical expenses	(-) 1,00,000	(-) 20,000
(iii) Animal trainer fees	(-) 50,000	(-) 15,000
(iv) Fodder expense	(-) 2,60,000	(-) 50,000
(v) Stable rent/insurance	(-) 1,20,000	(-) 36,000
(vi) Staff salaries	(-) 1,00,000	(-) 40,000
(vii) Depreciation in the value of horses—not allowed	—	—
	8,70,000	3,39,000
Less: Brought forward loss	6,00,000	Nil
	<u>2,70,000</u>	<u>3,39,000</u>
Total income of the firm = ₹ 6,09,000		

Note:

“Horse race” means a horse race upon which wagering or betting may be lawfully made [Explanation (b) to Sec. 74A]. Thus, where wagering or betting is not lawfully made on race horses, any loss incurred on such betting can neither be set-off nor carried forward. Hence, the carried forward loss of ₹ 2,00,000 cannot be set-off.

4. Mr N discloses the following incomes for the Previous Year 2011-2012 :

House property	Business or profession		Capital gains		Income from other sources
₹	Speculation ₹	Non-specu- lation ₹	STCG ₹	LTCG ₹	₹
A 50,000	P 3,00,000	X 5,00,000	C 6,00,000	F 7,00,000	Family pension 95,000
B (-) 40,000	S (-)2,00,000	Y (-) 3,00,000	D (-) 3,00,000	E (-)5,00,000	Loss from (-) 50,000 letting out from machinery / plant

Determine income under head of income for the A. Y. 2012-2013 :

Solution : Aggregation of income under each head of income: A. Y. 2012-2013

House property	Business or profession		Capital gains		Income from other sources
₹	Speculation ₹	Non-speculation ₹	STCG ₹	LTCG ₹	₹
A 50,000	P 3,00,000	X 5,00,000	C 6,00,000	F 7,00,000	Family pension 95,000
B (-)40,000	S (-)2,00,000	Y (-)3,00,000	D (-)3,00,000	E (-)5,00,000	Loss from (-)50,000 letting out machinery / plant
10,000	1,00,000	2,00,000	3,00,000	2,00,000	45,000



5. A discloses the following incomes from business or profession for the previous year 2011-2012:

	₹
(i) Profit from X business	6,00,000
(ii) Loss from Y business	(-) 2,00,000
(iii) Loss from profession Z	(-) 2,50,000
(iv) Profit from speculation business – M	2,00,000
(v) Loss from speculation business – N	(-) 3,00,000

Determine the income from business or profession for the assessment year 2012-2013

Solution : Income from business-profession for the AY 2012-2013

Particulars	₹
(i) X	6,00,000
(ii) Y	(-) 2,00,000
(iii) Z	(-) 2,50,000
Total Income from Non-Speculation Business and Profession	1,50,000
Income from Speculation Business	
(i) M	2,00,000
(ii) N	(-) 3,00,000
Loss from speculation business	(-) 1,00,000

Speculation loss cannot be set-off against the income from business profit, though both of them fall under the same head of income.

Thus, taxable business profits for the assessment year 2012-2013 is ₹ 1,50,000. The speculation loss will be carried forward for future set-off for 4 assessment years, immediately succeeding the assessment year for which it was first computed [Sec. 73(4)].

The time-limit of 4 years is applicable from the assessment year 2013-2014 and subsequent year.

6.D has earned income of ₹ 5,60,000 from speculation business during the PY 2011-2012. However, he has suffered losses in business and profession ₹ 3,20,000 and ₹ 1,70,000, respectively during the same period. Determine his income from business profession for the assessment year 2012-2013.

Solution : Income from business profession for the AY 2012-2013 :

Particulars	₹
Profits from speculation business	5,60,000
Less. (i) Loss from Non-Speculation Business	(-) 3,20,000
(ii) Loss from profession	(-) 1,70,000
Income from business and profession	70,000

STUDY NOTE - 11

DEDUCTION IN COMPUTING TOTAL INCOME

This Study Note includes

- Deductions (available under the Income Tax Act) from gross total income in order to arrive at taxable income.

INTRODUCTION

In order to further the government policy of attracting investment and activity in the desired direction and to provide stimulus to growth or to meet social objectives, concession in the form of 'deduction' from taxable income is allowed. Chapter VI-A of the Income-tax Act, 1961 contains such deduction provisions.

with the advent of new philosophy of giving direct assistance to the desired goal and avoiding indirect route of tax concessions, the number of deductions are being omitted. this is also with a view to avoid complexity of tax law.

In computing total income of an assessee deductions under sections 80CCC to 80U are permissible from "Gross total Income". [80A(1)]

Deduction not to be allowed unless return furnished [Sec. 80AC]

Where in computing the total income of an assessee of the previous year relevant to the assessment year commencing on the 1st day of April, 2006 or any subsequent assessment year, any deduction is admissible under section 80-IA or section 80-IAB or section 80-IB or section 80-IC or section 80-ID or section 80-IE, no such deduction shall be allowed to him unless he furnishes a return of his income for such assessment year on or before the due date specified under sub-section (1) of section 139.

"Gross total Income" means the aggregate of income computed under each head as per provisions of the Act, after giving effect to the provisions for clubbing of incomes (Sections 60 to 64) and set off of losses and but before making any deductions under this chapter. [Section 80B(5)]

The deductions under chapter VIA are not available from the following incomes though these are included in the "Gross total Income":

- long term Capital gains;
- winnings from lotteries, cross word puzzles etc.;
- incomes referred to in sections 115A to AD, 115BBA and 115D.

The aggregate amount of deductions under chapter VIA [Sections 80CCC to 80U] shall not exceed the "Gross total Income" of the assessee. [Section 80A(2)]

Deductions under Chapter VIA available for

I	II	III
In respect of expenditure or investment made by assessee [Sec. 80C to 80GGA]	In respect of certain income [Sec. 80HH to 80RRB]	Other deduction [Section 80U]

Deduction : Sec 80C : Deduction in respect of LIP, contributions to PF, etc:

1	Eligible Assessee	Individual and HUF
2	Condition	Investment or application of funds during the previous year
3	Maximum Deduction	₹. 1,00,000 in a previous year
4	Special Provisions	Withdrawal of deductions for certain premature exit from certain investments or application of funds

It is applicable to Individual and HUF and if the assessee has invested, contributed or expended in any one or more of listed items during the previous year. The deduction is available to the maximum extent of ₹ 1,00,000.



11.1 DEDUCTIONS FROM GROSS TOTAL INCOME

(a) Deduction in respect of certain investments, contributions, subscriptions etc.

Insertion of deduction under section 80C replacing rebates u/s 88, 88B, 88C, 88D deductions u/s 80CCC and u/s 80CCD

With effect from the 1st day of April, 2006, a new deduction u/s 80C has been introduced.

Rate of deduction [Section 80C(1)]

This deduction shall be admissible only to an assessee, being an individual or a Hindu undivided family. The amount of deduction shall be actual amount paid or deposited during the previous year in prescribed saving schemes [to be calculated as qualifying amount for deduction u/s 80c or ₹ 1,00,000 which ever is less.

Qualifying Amount For Deduction u/s 80C

- (i) to effect or to keep in force an insurance on the life of persons specified in sub-section (4);
- (ii) to effect or to keep in force a contract for a deferred annuity, not being an annuity plan referred to in clause (xii), on the life of persons specified in sub-section (4):

Provided that such contract does not contain a provision for the exercise by the insured of an option to receive a cash payment in lieu of the payment of the annuity;

- (iii) by way of deduction from the salary payable by or on behalf of the Government to any individual being a sum deducted in accordance with the conditions of his service, for the purpose of securing to him a deferred annuity or making provision for his spouse or children, in so far as the sum so deducted does not exceed one-fifth of the salary;
- (iv) as a contribution by an individual to any provident fund to which the Provident Funds Act, 1925 (19 of 1925) applies;
- (v) as a contribution to any provident fund set up by the Central Government and notified by it in this behalf in the Official Gazette, where such contribution is to an account standing in the name of any person specified in sub-section (4);
- (vi) as a contribution by an employee to a recognised provident fund;
- (vii) as a contribution by an employee to an approved superannuation fund;
- (viii) as subscription to any such security of the Central Government or any such deposit scheme as that Government may, by notification in the Official Gazette, specify in this behalf;
- (ix) as subscription to any such savings certificate as defined in clause (c) of section 2 of the Government Savings Certificates Act, 1959 (46 of 1959), as the Central Government may, by notification in the Official Gazette, specify in this behalf;
- (x) as a contribution, in the name of any person specified in sub-section (4), for participation in the Unit-linked Insurance Plan, 1971 (hereafter in this section referred to as the Unit-linked Insurance Plan) specified in Schedule II of the Unit Trust of India (Transfer of Undertaking and Repeal) Act, 2002 (58 of 2002);
- (xi) as a contribution in the name of any person specified in sub-section (4) for participation in any such unit-linked insurance plan of the LIC Mutual Fund [referred to in] clause (23D) of section 10, as the Central Government may, by notification in the Official Gazette, specify in this behalf;
- (xii) to effect or to keep in force a contract for such annuity plan of the Life Insurance Corporation or any other insurer as the Central Government may, by notification in the Official Gazette, specify;
- (xiii) as subscription to any units of any Mutual Fund [referred to in] clause (23D) of section 10 or from the Administrator or the specified company under any plan formulated in accordance with such scheme as the Central Government may, by notification in the Official Gazette, specify in this behalf;
- (xiv) as a contribution by an individual to any pension fund set up by any Mutual Fund [referred to in] clause (23D) of section 10 or by the Administrator or the specified company, as the Central Government may, by notification in the Official Gazette, specify in this behalf;

- (xv) as subscription to any such deposit scheme of, or as a contribution to any such pension fund set up by, the National Housing Bank established under section 3 of the National Housing Bank Act, 1987 (53 of 1987) (hereafter in this section referred to as the National Housing Bank), as the Central Government may, by notification in the Official Gazette, specify in this behalf;
- (xvi) as subscription to any such deposit scheme of—
 - (a) a public sector company which is engaged in providing long-term finance for construction or purchase of houses in India for residential purposes; or
 - (b) any authority constituted in India by or under any law enacted either for the purpose of dealing with and satisfying the need for housing accommodation or for the purpose of planning, development or improvement of cities, towns and villages, or for both,as the Central Government may, by notification in the Official Gazette, specify in this behalf;
- (xvii) as tuition fees (excluding any payment towards any development fees or donation or payment of similar nature), whether at the time of admission or thereafter,—
 - (a) to any university, college, school or other educational institution situated within India;
 - (b) for the purpose of full-time education of any of the persons specified in sub-section (4);
- (xviii) for the purposes of purchase or construction of a residential house property the income from which is chargeable to tax under the head “Income from house property” (or which would, if it had not been used for the assessee’s own residence, have been chargeable to tax under that head), where such payments are made towards or by way of—
 - (a) any instalment or part payment of the amount due under any self-financing or other scheme of any development authority, housing board or other authority engaged in the construction and sale of house property on ownership basis; or
 - (b) any instalment or part payment of the amount 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
 - (c) repayment of the amount borrowed by the assessee from—
 - (1) the Central Government or any State Government, or
 - (2) any bank, including a co-operative bank, or
 - (3) the Life Insurance Corporation, or
 - (4) the National Housing Bank, or
 - (5) any public company formed and registered in India with the main object of carrying on the business of providing long-term finance for construction or purchase of houses in India for residential purposes which is eligible for deduction under clause (viii) of sub-section (1) of section 36 or
 - (6) any company in which the public are substantially interested or any co-operative society, where such company or co-operative society is engaged in the business of financing the construction of houses, or
 - (7) the assessee’s employer where such employer is an authority or a board or a corporation or any other body established or constituted under a Central or State Act, or
 - (8) the assessee’s employer where such employer is a public company or a public sector company or a university established by law or a college affiliated to such university or a local authority or a co-operative society; or
 - (d) stamp duty, registration fee and other expenses for the purpose of transfer of such house property to the assessee,but shall not include any payment towards or by way of—
 - (A) the admission fee, cost of share and initial deposit which a shareholder of a company or a member of a co-operative society has to pay for becoming such shareholder or member; or
 - (B) the cost of any addition or alteration to, or renovation or repair of, the house property which is carried out after the issue of the completion certificate in respect of the house property by the authority competent to issue such certificate or after the house property or any part thereof has either been occupied by the assessee or any other person on his behalf or been let out; or
 - (C) any expenditure in respect of which deduction is allowable under the provisions of section 24;



- (xix) as subscription to equity shares or debentures forming part of any eligible issue of capital approved by the Board on an application made by a public company or as subscription to any eligible issue of capital by any public financial institution in the prescribed form

Explanation — For the purposes of this clause,—

- (i) “eligible issue of capital” means an issue made by a public company formed and registered in India or a public financial institution and the entire proceeds of the issue are utilised wholly and exclusively for the purposes of any business referred to in sub-section (4) of section 80-IA
- (ii) “public company” shall have the meaning assigned to it in section 3 of the Companies Act, 1956 (1 of 1956);
- (iii) “public financial institution” shall have the meaning assigned to it in section 4A of the Companies Act, 1956 (1 of 1956);
- (xx) as subscription to any units of any mutual fund referred to in clause (23D) of section 10 and approved by the Board on an application made by such mutual fund in the prescribed form
- (xxi) *as term deposit*—
 - (a) *for a fixed period of not less than five years with a scheduled bank; and*
 - (b) *which is in accordance with a scheme^{27a} framed and notified, by the Central Government, in the Official Gazette for the purposes of this clause.*
- (xxii) as subscription to such bonds issued by the National Bank for Agriculture and Rural Development, as the Central Government may, by notification in the Official Gazette, specify in this behalf.

Taxability of Amount Received

1. In following cases the assessee shall have to pay tax on any amount received on:

- (i) Termination of his contract of insurance referred to at point I above by notice to that effect or where the contract ceases to be in force by reason of failure to pay any premium, by not reviving contract of insurance :
 - (a) in case of any single premium policy, within two years after the date of commencement of insurance; or
 - (b) in any other case, before premiums have been paid for two years; or
- (ii) termination of his participation in any unit-linked insurance plan referred to above in point 10 and 11 by notice to that effect or where he ceases to participate by reason of failure to pay any contribution, by not reviving his participation, before contributions in respect of such participation have been paid for five years; or
- (iii) transfer of the house property before the expiry of five years from the end of financial years in which possession of such property is obtained by him, or receives back, whether by way of refund or otherwise, any sum specified in that clause, then :
 - (a) no deduction shall be allowed to the assessee under 80C(I) with reference to any of the sums referred to in point 1, 10, 11 and 18, paid in such previous year; and
 - (b) the aggregate amount of the deductions of income so allowed in respect of the previous year or years shall be deemed to be the income of the assessee of such previous year and shall be liable to tax in the assessment year relevant to such previous year.

DEDUCTION IN RESPECT OF CONTRIBUTION TO PENSION FUND OF LIC OR ANY OTHER PENSION FUND [Sec. 80CCC]

1	Eligible Assessee	Individual
2	Condition	Investment or application of funds during the previous year
3	Maximum Deduction	₹ 1,00,000 in a previous year
4	Special Provisions	Withdrawal of deductions for certain premature exit from certain investments or application of funds

Deduction of a maximum amount of ₹ 100,000 is allowed to an individual assessee for the amount paid or deposited by the assessee during previous year (out of his taxable income upto assessment year 2002-03) to effect or keep in force a contract for annuity plan of LIC or any other insurer for receiving pension from the fund referred to

in s. 10(23AAB). The whole of the amount received by an assessee or his nominee shall be taxable in the year in which the amount is so received. It may be mentioned that where deduction is claimed in respect of any amount paid or deposited, under this section, no rebate u/s.88 shall be allowed with reference to the same amount. However, any payment in commutation of pension received from the fund referred to in section 10(23AAB) is exempt [u/s.10(10A)(iii)].

Deduction u/s 80CCC for investment in pension funds.

Where any amount paid or deposited by the assessee has been taken into account for the purposes of this section :

- (a) a rebate with reference to such amount shall not be allowed under sec 88 for any assessment year ending before the 1st day of April , 2006;
- (b) a deduction with reference to such amount shall not be allowed under section 80C for any assessment year beginning on or after the 1st day of April, 2006.

Deduction u/s 80CCD for contribution to pension scheme of Central Government

1	Eligible Assessee	Individual
2	Condition	Investment or application of funds during the previous year
3	Maximum Deduction	Up to 10% of his salary subject to maximum of ₹ 1,00,000
4	Special Provisions	Withdrawal of deductions for certain premature exit from certain investments or application of funds

Where any amount paid or deposited by the assessee has been allowed as a deduction under this section:

- (a) No rebate with reference to such amount shall be allowed under section 88 for any assessment year ending before the 1st day of April ,2006;
- (b) No deduction with reference to such amount shall be allowed under section 80C for any assessment year beginning on or after the 1st day of April ,2006.

Tax benefits for New Pension System - extended also to “self-employed”, and tax treatment of savings under this system as “exempt-exempt-taxed” [Section 10(44), 115-0,197A and 80CCD W.r.e.f. A.Y. 2009-10]

Amendment in section 80CCD: The tax benefit under section 80CCD of the Income-tax Act, 1961 was hitherto available to “employees” only. However, the NPS now has been extended also to “self-employed”. Therefore, the Act has also amended sub-section (1) of section 80CCD so as to extend the tax benefit thereunder also to “self-employed” individuals.

Further, in the case of an employee of Central Government or of any other employer, the deduction of employees’ contribution shall be limited to 10% of his salary. Whereas in the case self-employed persons, it shall be limited to 10% of his Gross Total Income in the previous year.

Note : The Act has also inserted sub-section (5) to section 80CCD to provide that for the purposes of the said section the assessee shall be deemed not to have received any amount In the previous year If such amount Is used for purchasing an annuity plan In the same previous year.

Section 80CCE

The aggregate amount of deductions under Sec. 80C, Sec. 80CCC and Sec. 80CCD shall not, in any case, exceed one lakh rupees.

Sec. 80CCF : Deduction in respect of subscription to long-term infrastructure bonds :

1	Eligible Assessee	Individual and HUF
2	Condition	Subscription paid or deposited in notified long-term infrastructure bonds
3	Maximum Deduction	₹ 20,000.

DEDUCTION IN RESPECT OF MEDICAL INSURANCE PREMIA [Sec.80D]

1	Eligible Assessee	Individual and HUF
2	Condition	Investment or application of funds during the previous year by any mode of payment other than cash
3	Maximum Deduction	₹ 15,000. If they medical insurance premia is paid for senior citizen, then maximum deduction is up to ₹ 20,000

Deduction is allowed for any medical insurance premium **paid by any mode of payment other than cash** out of assessee's taxable income to GICI or any other approved insurer during the previous year, upto a maximum amount of ₹ 15,000. The deduction is allowed in respect of the following :-

- In case of an individual – insurance on the health of the assessee or wife or husband, dependent parents or dependent children.
- In case of a HUF – insurance on the health of any member of the family.

However, where the assessee or his wife or her husband or dependent parents or any member of his family of HUF is a senior citizen, the limit of deduction is raised from ₹ 15,000 to ₹ 20,000

DEDUCTION IN RESPECT OF MEDICAL TREATMENT OF HANDICAPPED DEPENDENT [Sec. 80DD]

Section 80DD of the Income Tax Act provides for a deduction to an individual or HUF, who is a resident in India, in respect of the following:

- Expenditure for the medical treatment (including nursing), training and rehabilitation of a dependant, being a person with disability; and
- Amount paid to LIC or other insurance in respect of a scheme for the maintenance of a disabled dependant.

1	Eligible Assessee	Individual and HUF
2	Condition	Expenditure for medical treatment during the previous year
3	Maximum Deduction	₹ 50,000, but where dependent is a person with servere disability, maximum deduction is ₹ 1,00,000.

Deduction is available to resident individual or HUF:

- For any expenditure incurred by an assessee during the previous year, for the medical treatment (including nursing) training and rehabilitation of handicapped dependent.
- amount paid or deposited under any scheme framed by LIC and which is approved by CBDT and out of Income chargeable to tax for the maintenance of handicapped dependent. From the assessment year 2000-01 a straight deduction of ₹ 40,000 is allowed irrespective of actual expenditure incurred/amount deposited. If the handicapped dependent predeceases the individual or the member of HUF in whose name money has been deposited, an amount equal to the amount paid or deposited under the scheme shall be deemed to be the income of the assessee of the previous year in which sum amount is received by the assessee and chargeable to tax in that previous year.

For the purpose of this section dependent means a person who is not dependent for the suspect or main term on any person other than the assessee.

DEDUCTION IN RESPECT OF MEDICAL TREATMENT, ETC. [Sec 80DDB]

1	Eligible Assessee	Individual and HUF
2	Condition	The amount should be actually paid for the medical treatment of specified diseae.
3	Maximum Deduction	₹ 40,000 but if the amount paid is for senior citizen then the ceiling limit is ₹ 60,000
4	Special Provisions	The assessee is required to furnish with the return of income, a certificate is prescribed form No. 10-I.

Deduction is allowed to a resident individual or Hindu undivided family in respect of expenditure actually during the P.Y. incurred for the medical treatment of specified disease or ailment as specified in the Rules 11DD for himself or a dependent relative or a member of a HUF.

Conditions :

- (i) The assessee has to furnish a certificate in form 10 – I from any doctor registered with Indian Medical Association with postgraduate qualifications.
- (ii) “Dependent” means a person who is dependent for his support or maintenance on the assessee and on no other person.

a deduction of ₹ 40,000 is allowed irrespective of actual amount of expenditure as reduced by the amount received if any, from an insurer for the medical treatment of such person.

Specified diseases and ailments under section 80DDB and Rule 11DD –

- (i) Neurological Diseases i.e.
 - (a) Dementia;
 - (b) Dystonia Musculorum Deformans
 - (c) Motor Neuron Disease;
 - (d) Ataxia;
 - (e) Chorea;
 - (f) Hemiballismus
 - (g) Aphasia
 - (h) Parkinsons Disease
- (ii) Cancer
- (iii) AIDS
- (iv) Chronic Renal Failure
- (v) Hemophilia
- (vi) Thalassaemia

DEDUCTION IN RESPECT OF INTEREST ON LOAN TAKEN FOR HIGHER EDUCATION [Section 80E]

1	Eligible Assessee	Individual
2	Condition	The amount is paid by the assessee out of his income as interest on loan taken for higher education.
3	Maximum Deduction	100% of the interest paid on loan taken without any monetary ceiling limit.
4	Special Provisions	The assessee can claim the amount of interest in the initial assessment year & carry forward up to 7 assessment years.

In computing the total income of an assessee, being an individual, there shall be deducted, in accordance with and subject to the provisions of this section, any amount paid by him in the previous year, out of his income chargeable to tax, by way of interest on loan taken by him from any financial institution or any approved charitable institution for the purpose of higher education of his relative [Section 80E(1)]

The deduction specified above shall be allowed in computing the total income in respect of the initial assessment – year and seven assessment years immediately succeeding the initial assessment year or until the interest referred above is paid by the assessee in full, whichever is earlier [80E(2)]

Meaning of “relative” enlarged: The Act has enlarged the definition of “relative” given in clause (e) of sub-section (3). As per the new definition “relative”, in relation to an individual, means the spouse and children of that individual or the student for whom the individual is the legal guardian.



DEDUCTION IN RESPECT OF DONATIONS TO CERTAIN FUNDS, CHARITABLE INSTITUTIONS, ETC. [Sec. 80G]

1	Eligible Assessee	Individual
2	Condition	The amount is paid by the assessee out of his income as interest on loan taken for higher education.
3	Maximum Deduction	100% of the interest paid on loan taken without any monetary ceiling limit.
4	Special Provisions	The assessee can claim the amount of interest in the initial assessment year & carry forward up to 7 assessment years.

Deduction under this section is available to all assessees.

Conditions for claiming deduction

- (i) the donation should be of a sum of money and not in kind
- (ii) the donation should be to specified funds/institutions.

<i>Eligible Donation amount</i>	<i>Qualifying deduction</i>	<i>Permissible</i>
<ol style="list-style-type: none"> 1. PM's National Relief Fund; 2. PM's Armenia Earthquake Relief Fund; 3. The Africa (Public Contributions India) Fund; 4. The national foundation for communal Harmony 5. A university or any educational institution of national eminence as may be approved; 6. The National Illness Assistance Fund; 7. Any Zila Saksharta Samiti for improvement of primary education in villages and towns and for literacy activities; 8. National Blood Transfusion Council or to any State Blood Transfusion Council; 9. Any fund set up by the State Government for medical relief to the poor; 10. The Army Central Welfare Fund or the Indian Naval Benevolent Fund or the Airforce Central Welfare Fund established by the armed forces of the Union for the welfare of the past and present members of the such forces or their dependants; 11. The Chief Minister's Relief Fund or the Lieutenant Governor's Relief Fund in respect of any State or Union Territory, as the case may be; 	<p>From item Nos. 1 to 23 there is no maximum limit (i.e. 100% of the amount will qualify for deduction)</p>	<p>Quantum of deduction for item Nos. 1 to 18, 24 & 30 = 100% of the qualifying amount.</p> <p>For other items, quantum of deductions = 50% of the qualifying amount.</p>

<ol style="list-style-type: none"> 12. The National sports Fund to be set up by the Central Government; 13. The National Cultural Fund set up by the Central Government; 14. The Fund for Technology Department and Application setup by the Central Government; 15. The National Defence Fund; 16. Any fund setup by the State Government of Gujarat exclusively for providing relief to the victims of earthquake in Gujarat; 17. Any sum paid during the period beginning with 26.1.2001 and ending on 30.9.2001 to any trust, institutions or fund recognised under section 80G for providing relief to the victims of earthquake in Gujarat; 18. National Trust for Welfare of Persons with Autism, Cerebral Palsy, Mental Retardation and Multiple disabilities constituted under the relevant Act of 1999; 19. PM's Drought Relief Fund; 20. The National Children's fund; 21. Jawaharlal Nehru Memorial fund; 22. Indira Gandhi Memorial Trust; 23. Rajiv Gandhi foundation; 24. Contribution by a company as donations to the Indian Olympic Association or to any other Association notified by the Central Government u/s. 10(23); 25. Any approved fund or institution established for charitable purposes; 26. Government or local authority to be used for charitable purpose; 27. Any authority set up for providing housing accommodation or town planning; 28. Any corporation established by government for promoting interest of schedules caste/scheduled tribe/backward class; 29. Renovation of notified temple mosque, church, or gurudwara or any other notified place of national importance; 30. Government or local authority or approved institution/association for promotion of family planning; 	<p>From Sl. Nos. 24 to 30 qualifying amount shall be restricted to 10% of adjusted total income (i.e. G.T.I. as reduced by deductions u/s. 80CCC to 80U other than 80G and other income on which no tax is payable and other incomes on which deductions under chapter VIA are not allowed)</p>	
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DEDUCTION IN RESPECT OF RENTS PAID [SEC. 80GG]

1	Eligible Assessee	Individual
2	Condition	The condition for deduction in respect of rents paid is given below.
3	Maximum Deduction	Amount of deduction is also given below.

The deduction in respect of rent paid is available to Individual with effect from assessment year 1998-99.

Conditions :

- The assessee is not being in receipt of any house rent allowance following under clause (13A) of section 10 from his employer.
- The expenditure incurred (for the purpose of his own residence) by way of rent for any furnished or unfurnished accommodation is in excess of 10% of his total Income after allowing all deductions except deduction under this section.
- The assessee or his spouse or minor child or an HUF of which he is a member does not own any accommodation at the place where he ordinarily resides or performs duties of his office or employment or carries on his business/profession.
- If the assessee owns any accommodation at any place other than the place of employment or business and such accommodation is not in the occupation of the assessee and shall not be assessed in his hands as self occupied property.

Deduction : Least of the following :-

- Rent paid minus 10% of adjusted total income
- 25% of adjusted total income
- ₹ 2,000 p.m.

Adjusted Total income : Gross Total Income as reduced by :

- Long term Capital gain, if any, included in the Gross Total Income
- all deduction under chapter VIA (Section 80CCC to 80U) other than the deduction under this section.
- any income referred to in sections 115A to D included in the Gross Total Income.

DEDUCTION IN RESPECT OF CERTAIN DONATIONS FOR SCIENTIFIC RESEARCH OR RURAL DEVELOPMENT [Sec. 80GGA]

In computing the total income of an assessee whose gross total income does not include income from "Profits and gains of business or profession", deduction shall be allowed of an amount paid by him to—

- an approved scientific research association or University or College or other institution to be used for scientific research, research in social science or statistical research.
- an approved association or institution to be used for carrying out any approved programme or rural development, an approved institution, association or which has the object of training of persons for implementing programmes of rural development 35CCA
- public sector company or local authority or an approved association or institution for carrying out any eligible project or scheme 35AC.
- association/institution/fund which has the object of carrying out any programme of conservation of natural resources or sec. 35CCB afforestation.
- National Urban Poverty Eradication Fund (NUPEF).

DEDUCTIONS BY COMPANIES TO POLITICAL PARTIES [Sec 80GGB]

Allowable to : An Indian Company

Amount of Deduction : 100% of sum contributed during a previous year to any political party, registered u/s 29A of Representation of the People Act, 1951.

DONATIONS TO POLITICAL PARTIES [Sec. 80GGC]

Allowable to : Any person except local authority and an artificial juridical person wholly or partly funded by the Government.

Amount of Deduction: 100% of sum contributed during a previous year to any political party, registered u/s 29A of Representation of the People Act, 1951.

Contributions to an Electoral Trust also eligible for deduction under section 80GGB and 80GGC

DEDUCTIONS IN RESPECT OF PROFITS & GAINS FROM INDUSTRIAL UNDERTAKINGS OR ENTERPRISES ENGAGED IN INFRASTRUCTURE DEVELOPMENT [Sec. 80IA]

The deduction under this section is applicable to all assesseees whose Gross Total Income includes any profits and gains derived from any business of an industrial undertaking or an enterprise as below :

Sl. No.	Classification of Industries	Period of commencement	Deduction
(i)	Any enterprise carrying on the business of developing or maintaining and operating or developing, maintaining and operation any infrastructure facility	On or after 1.4.1995	100% for 10 consecutive Assessment Yrs.
(ii)	Any undertaking providing telecommunication services whether basic or cellular including radio paging, domestic satellite service or network of trunking and electronic data interchange services.	1.4.95 and 31.3.2003	100% for first 5 yrs & 30% for companies & 25% for others for the next 5 yrs.
(iii)	Any undertaking which develops, develops and operates or maintains and operates an industrial park notified by the Central Government.	1.4.97 and 31.3.2002	100% for 10 consecutive assessment years.
(iv)	An Industrial undertaking set up in any part of India for the generation or generation and distribution of power.	1.4.93 and 31.3.2003	100% for 10 consecutive assessment years.
(v)	An industrial undertaking which starts transmission 31.3.2003 or distribution of power by laying a network of new transmission or lays and begins to operate a cross-country natural gas distribution network.	1.4.99 and	100% for 10 consecutive assessment years.

The deduction under this section is available at the option of the assessee for any 10 consecutive assessment years out of 15 years beginning from the year in which the undertaking or enterprise develops and begins to operate any infrastructure facility or starts providing telecommunication services or develops an industrial part or generates power or commences transmission or distribution of power. However, in case of an infrastructure facility being a high way project including housing or other activities being an integral part of a high way project, the assessee can claim deduction for any 10 consecutive assessment years out of 20 years beginning from the year of operation.

Other Conditions :

- For the purpose of completing deduction under this section, the profits and gains of the eligible business shall be computed as if such eligible business were the only source of income during the relevant previous year.



- (ii) Where housing or other activities are an integral part of the high way project and the profits and gains of which have been calculated in accordance of the provision of the section, the profits have not been liable to tax if the following conditions are not fulfilled :-
 - (a) The profits have been transferred to a special reserve account
 - (b) The same is actually utilised for the high way project excluding housing and other activities before the expiry of 3 years following the year of transfer to the reserve account.
 - (c) The amount remaining unutilised shall be chargeable to tax as income of the year in which such transfer to reserve account took place
- (iii) Where the assessee is a person other than a company or a cooperative society, the deduction shall not be admissible unless the accounts of the industrial undertaking for the previous year relevant to the assessment year for which the deduction is claimed have been audited by an accountant and his report in form No. 10CCB (Rule 18BBB) is furnished alongwith the return of income.
- (iv) Where any goods or services held for purposes of the eligible business are transferred to any other business carried on by the assessee or vice versa and if the consideration for such transfer does not correspond to the market value of such goods or services as on the date of transfer, the profits and gains of the eligible business shall be computed as if the transfer had been made at the market value of such goods or services as on that date however if the computation of profits and gains presents any difficulty in the opinion of the assessing officer, he may compute such profits and gains on such reasonable basis as he may deem feed. Similarly, Where due to close connection between the assessee and other person for any other reason it appears to the assessing officer that the profits of the eligible business is increased to more than the ordinary profit the assessing officer shall compute the profit on a reasonable basis for allowing the deduction.
- (v) If the profits and gains are allowed as deduction under this section for any assessment year, no deduction under sections 80HH to 80RRA to the extent of such profits and gains shall be allowed.
- (vi) Where any undertaking of an Indian company which is entitled the deduction under this section is transferred before expiry of the period of deduction to another Indian company in a scheme of amalgamation or demerger, no deduction has been admissible to the amalgamating or demerged company for the previous year in which amalgamation or demerger expressed and the amalgamated or the resulting company shall be entitled to the deduction as if the amalgamation or demerger had not taken place.

Amendments in section 80-IA

(A) Extension of sunset clause for undertakings engaged in development of industrial park [Section 8(IA(3)) [W.e.f. A.Y. 2009-10]

Under the existing provisions, in case of an undertaking which develops, develops and operates or maintains and operates an industrial park, deduction under section 80-1A is available if it commences its business before 31-3-2009. The Finance (No. 2) Act, 2009 has extended the terminal date from 31-3-2009 to 31-3-2011.

Section 80IA(4) : Extension of tax benefits for developing, operating, maintaining an infrastructure facility to authorities constituted under a Central or State Act.

The Act has amended section 80-IA(4) so as to enable an authority or a board or a corporation or any other body established or constituted under a Central or State Act which is not incorporated under the Companies Act, 1956 also to take advantage of the benefits provided under the said section.

The ordinance has extended the tax benefits under section 80-IA to an undertaking owned by an Individual company set up for re-construction or revival of a power generating plant if the following conditions are satisfied :

- Such undertaking must be owned be an Indian company.
- Such Indian company is formed before 30-11-2005 with majority equity participation by public sector companies for the purposes of enforcing the security interest of the lenders to the company owning the power generating plant.
- Such Indian company is notified before 31-12-2005 by the Central Government for the purposes of this clause.
- Such undertaking begins to generate or transmit or distribute power before 31-03-2007.

(B) Extension of sunset clause for tax holiday under section 80-IA to extend the terminal date for commencing the activity of generation, transmission or distribution of power in case of an undertaking owned by an Indian company and set up for reconstruction or revival of a power generating plant before 31-12-2005 [Section 80-IA(4)]

Under the existing provisions of section 80-IA(4)(v), an undertaking owned by an Indian company and set up for reconstruction or revival of a power generating plant is eligible for 10 year tax benefit if it fulfils the following conditions :—

- (i) Such company is formed before 30-11-2005 with majority equity participation by public sector companies for enforcing the security interest of the lenders to the company owning the power generating plant;
- (ii) Such Indian company is notified by the Central Government before 31-12-2005; and
- (iii) The undertaking begins to generate or transmit or distribute power before 31-3-2008.

The Act has amended sub-clause (b) of clause (v) of sub-section (4) of section 80-IA to extend the terminal date for commencing the activity of generation, transmission or distribution of power in case of such undertaking from 31-3-2008 to 31-3-2011.

Deductions in respect of profits and gains by an undertaking or enterprise engaged in development of Special Economic Zone [Sec. 80IAB]

- (1) Where the gross total income of an assessee, being a Developer, includes any profits and gains derived by an undertaking or an enterprise from any business of developing a Special Economic Zone, notified on or after the 1st day of April, 2005 under the Special Economic Zones Act, 2005, there shall, in accordance with and subject to the provisions of this section, be allowed, in computing the total income of the assessee, a deduction of an amount equal to one hundred per cent of the profits and gains derived from such business for ten consecutive assessment years.
- (2) The deduction specified in sub-section (1) may, at the option of the assessee, be claimed by him for any ten consecutive assessment years out of fifteen years beginning from the year in which a Special Economic Zone has been notified by the Central Government :

Provided that where in computing the total income of any undertaking, being a Developer for any assessment year, its profits and gains had not been included by application of the provisions of sub-section (13) of section 80-IA, the undertaking being the Developer shall be entitled to deduction referred to in this section only for the unexpired period of ten consecutive assessment years and thereafter it shall be eligible for deduction from income as provided in sub-section (1) or sub-section (2), as the case may be :

Provided further that in a case where an undertaking, being a Developer who develops a Special Economic Zone on or after the 1st day of April, 2005 and transfers the operation and maintenance of such Special Economic Zone to another Developer (hereafter in this section referred to as the transferee Developer), the deduction under sub-section (1) shall be allowed to such transferee Developer for the remaining period in the ten consecutive assessment years as if the operation and maintenance were not so transferred to the transferee Developer.

- (3) The provisions of sub-section (5) and sub-sections (7) to (12) of section 80-IA shall apply to the Special Economic Zones for the purpose of allowing deductions under sub-section (1).

DEDUCTION IN RESPECT OF PROFITS AND GAINS FOR CERTAIN INDUSTRIAL UNDERTAKING OTHER THAN INFRASTRUCTURE DEVELOPMENT UNDERTAKINGS [Sec. 80IB]

The deduction is available to the following undertaking or enterprises etc.

Sl. No.	Undertaking	% of Profit deductible	Period of deduction
A.	Ship- brought into use between 1.4.91 & 31.3.95	30	10 years
B.	Hotel-commenced between 1.4.97 and 31.3.2001 approved hotel in hilly are or rural area or a place of pilgrimage or in a notified area	50	10 years
C.	Any other approved hotel (Hotels in the cities of Calcutta, Chennai, Delhi and Mumbai are not eligible).	50	10 years

Sl No.	Classification of Industries	Period of Commencement between	Deduction of profits dividend
1	Industrial undertaking located in an industrially backward state specified in the Eighth schedule; (see note No. 3 below the table)	1.4.93 and 31.3.2002	100%. for initial 5 yrs. Thereafter 30% for 5 years. In case of company otherwise 25%. For cooperative society deduction is 100% of initial 5 years and thereafter 25% of 7 years.
2	Industrial undertaking located in industrially backward district notified by the Central Government -Category A -Category B	1.4.94 and 31.3.2002	100% for 5 yrs and 30% for next 5 yrs. 100% for 3 years and 30% for next 5 yrs in case of company (25% for others). For cooperative society 25% for 7 yrs. in both the category after initial 5 years.
3	Any company engaged in scientific and industrial research and development.	Approved by the prescribed authority after business for 31.3.2000 but before 1.4.2003	100% of the profits derived from such business for 10 years.
4	Undertaking which begins commercial production of mineral oil – a) in North Eastern Region. b) in other Regions Undertaking which begins refining of mineral oil.	Before 1.4.97 on or after 1.4.97. On or after 1.10.98	100% for the first 7 consecutive assessment years including the initial assessment years.
5	Undertaking engaged in developing and building housing projects approved by a local authority – size profits derived from of the plot of land minimum 1 acre and residential unit built up of 1000 sq. ft. where such residential units other than cities of Delhi/Mumbai or within 25 kms. for the municipal limits of these cities and 1500 sq. ft. at any other place.	1.10.98 and 31.03.2003	100% of the profit derived from such business.
6	Industrial undertaking deriving profit from the business of setting up and operating a cold chain facility for agricultural produce.	1.4.99 and 31.03.2003	100% for initial 5 yrs. and thereafter 30% for 5 years in case of company (25% for others). For Co-operative Society cooperative society after initial 5 yrs 100%, 7 years @ 25%
7	Undertaking engaged in integrated business of handling, storage and transportation of food grains.	On or after 1.04.2001	100% for initial 5 yrs. Thereafter 30% for 5 years for company (25% for others).

E	Finance Act, 2002, inserted Sec. 80IB(7A) and Sec.80IB(7B) allowing deduction in case of any multiplex theatre and convention centers w.e.f. AY 2003-04 as under : - Multiplex theatre - Convention Centre	1.4.2007 and ending 31.3.2012	50% of the profits of 5 consecutive years beginning from the initial assessment year.
		1.4.2007 and ending 31.3.2012	50% of the profits of 5 consecutive years beginning from the initial assessment year.

Section 80-IB (4) :

Extension of time limit for setting up of industries in the State of Jammu and Kashmir for the purpose of tax holiday : With a view to promote the industrial development of the State of Jammu and Kashmir the Finance Act, 2005 has extended the terminal date for setting up of industrial undertakings and commencement of eligible business in the State by two more years, from 31-03-2005 to 31-03-2007.

Section 80-IB(8A) :

Extension of the time limit for the purpose of tax holiday to any company carrying on scientific research and development : The Finance Act, 2005 has amended section 80-IB(8A) so as to allow the deduction to companies carrying on scientific research and development, which are approved by the prescribed authority before 1- 4-2007.

Amendments in section 80-IB

- (A) Rationalising the provisions of deduction under section SO-IB(IO) developing and building housing projects - Not to apply to any undertaking which executes the housing project as a works contract awarded by any other person (including Central or State Government) [Section 80-IB(10)]

Sub-section (10) of section 80-IB of the Income-tax Act, 1961 provides for 100% deduction of the profits derived by an undertaking from developing and building housing projects, This benefit is available subject to the following conditions:

- The project is approved by a local authority before 31-3-2007. (See amendment below).
- The project is constructed on a plot of land having a minimum area of one acre.
- The built-up area of each residential unit should not exceed 1,000 sq. ft. in the cities of Delhi and Mumbai (including areas falling within 25 kms. of municipal limits of these cities) and 1,500 sq. ft. in other places.
- The built-up area of the shops and other commercial establishments included in the housing project should not exceed 5% of the total built-up area of the housing project or 2,000 sq. ft. whichever is less.
- The project has to be completed within 4 years from the end of the financial year in which the project is approved by the local authority.

The objective of this tax concession is to provide tax benefit to the person undertaking the investment risk i.e. the actual developer. However, any person undertaking pure contract risk is not entitled to the tax benefits.

With a view to clarify accordingly, the Act has inserted an Explanation after subsection (10) of section 80-IB so as to provide that nothing contained in this sub-section shall apply to any undertaking which executes the housing project as a works contract awarded by any other person (including Central or State Government).

This amendment will take effect retrospectively from 1-4-2001 and shall accordingly, apply in relation to assessment year 2001-02 and subsequent assessment years.

Further, the objective of the tax benefit for housing projects is to build housing stock for low and middle income households. This has been ensured by limiting the size of the residential unit. However, this is being circumvented by the developer by entering into agreement to sell multiple adjacent units to a single buyer. Accordingly, the Act has inserted new clauses viz. clause (e) and (/) to section 80-18(10) to provide that the undertaking which develops and builds the housing project shall not be allowed to allot more than one residential unit in the housing project to the same person, not being an individual, and where the person is an individual, no other residential unit in such housing project is allotted to any of the following person:—



- (i) The individual or the spouse or minor children of such individual;
- (ii) The Hindu undivided family in which such individual is the karta;
- (iii) Any person representing such individual, the spouse or minor children of such individual or the Hindu undivided family in which such individual is the karta.

This amendment will take effect from 1-4-2010 and shall accordingly, apply in relation to assessment year 2010-11 and subsequent years.

Further, as per the Finance (No. 2) Act, 2009 the deduction will be available if the project is approved by the local authority before 31-3-2008 instead of 31-3-2007.

- (B) Deduction available under section 80-IB relating to undertaking engaged in the business of processing, preservation and packaging of fruits or vegetables or integrated business of handling, storage and transportation of food grains also extended to certain other products [Section 80-113(11A)] [W.e.f. A.Y. 2010-11]

Under the existing provisions of section 80-18(11 A) deduction is available to an undertaking engaged in the business of processing, preservation and packaging of fruits or vegetables or integrated business of handling, storage and transportation of food grains. The Finance (No. 2) Act, 2009 has extended the benefits to an undertaking deriving profits from the business of processing, preservation and packaging of meat and meat products or poultry or marine or dairy products.

The provisions of this section shall not apply to an undertaking engaged in the business of processing, preservation and packaging of meat or meat products or poultry or marine or dairy products if it begins to operate such business before 1-4-2009.

Special provisions in respect of certain undertakings or enterprises in certain special category States [Sec. 80-IC]

- (1) Where the gross total income of an assessee includes any profits and gains derived by an undertaking or an enterprise from any business referred to in sub-section (2), there shall, in accordance with and subject to the provisions of this section, be allowed, in computing the total income of the assessee, a deduction from such profits and gains, as specified in sub-section (3).
- (2) This section applies to any undertaking or enterprise,—
 - (a) which has begun or begins to manufacture or produce any article or thing, not being any article or thing specified in the Thirteenth Schedule, or which manufactures or produces any article or thing, not being any article or thing specified in the Thirteenth Schedule and undertakes substantial expansion during the period beginning—
 - (i) on the 23rd day of December, 2002 and ending before the 1st day of April, 2012, in any Export Processing Zone or Integrated Infrastructure Development Centre or Industrial Growth Centre or Industrial Estate or Industrial Park or Software Technology Park or Industrial Area or Theme Park, as notified by the Board in accordance with the scheme framed and notified by the Central Government in this regard, in the State of Sikkim; or
 - (ii) on the 7th day of January, 2003 and ending before the 1st day of April, 2012, in any Export Processing Zone or Integrated Infrastructure Development Centre or Industrial Growth Centre or Industrial Estate or Industrial Park or Software Technology Park or Industrial Area or Theme Park, as notified by the Board in accordance with the scheme framed and notified by the Central Government in this regard, in the State of Himachal Pradesh or the State of Uttaranchal; or
 - (iii) on the 24th day of December, 1997 and ending before the 1st day of April, 2012, in any Export Processing Zone or Integrated Infrastructure Development Centre or Industrial Growth Centre or Industrial Estate or Industrial Park or Software Technology Park or Industrial Area or Theme Park, as notified by the Board in accordance with the scheme framed and notified by the Central Government in this regard, in any of the North-Eastern States;
 - (b) which has begun or begins to manufacture or produce any article or thing, specified in the Fourteenth Schedule or commences any operation specified in that Schedule, or which manufactures or produces any article or thing, specified in the Fourteenth Schedule or commences any operation specified in that Schedule and undertakes substantial expansion during the period beginning—

- (i) on the 23rd day of December, 2002 and ending before the 1st day of April, 2012, in the State of Sikkim; or
 - (ii) on the 7th day of January, 2003 and ending before the 1st day of April, 2012, in the State of Himachal Pradesh or the State of Uttaranchal; or
 - (iii) on the 24th day of December, 1997 and ending before the 1st day of April, 2012, in any of the North-Eastern States.
- (3) The deduction referred to in sub-section (1) shall be—
- (i) in the case of any undertaking or enterprise referred to in sub-clauses (i) and (iii) of clause (a) or sub-clauses (i) and (iii) of clause (b), of sub-section (2), one hundred per cent of such profits and gains for ten assessment years commencing with the initial assessment year;
 - (ii) in the case of any undertaking or enterprise referred to in sub-clause (ii) of clause (a) or sub-clause (ii) of clause (b), of sub-section (2), one hundred per cent of such profits and gains for five assessment years commencing with the initial assessment year and thereafter, twenty-five per cent (or thirty per cent where the assessee is a company) of the profits and gains.
- (4) This section applies to any undertaking or enterprise which fulfils all the following conditions, namely:—
- (i) *it is not formed by splitting up, or the reconstruction, of a business already in existence :*

Provided that this condition shall not apply in respect of an undertaking which is formed as a result of the re-establishment, reconstruction or revival by the assessee of the business of any such undertaking as is referred to in section 33B, in the circumstances and within the period specified in that section;

- (ii) it is not formed by the transfer to a new business of machinery or plant previously used for any purpose.

Explanation : The provisions of *Explanations 1* and *2* to sub-section (3) of section 80-IA shall apply for the purposes of clause (ii) of this sub-section as they apply for the purposes of clause (ii) of that sub-section.

- (5) Notwithstanding anything contained in any other provision of this Act, in computing the total income of the assessee, no deduction shall be allowed under any other section contained in Chapter VIA or in section 10A or section 10B, in relation to the profits and gains of the undertaking or enterprise.
- (6) Notwithstanding anything contained in this Act, no deduction shall be allowed to any undertaking or enterprise under this section, where the total period of deduction inclusive of the period of deduction under this section, or under the second proviso to sub-section (4) of section 80-IB or under section 10C, as the case may be, exceeds ten assessment years.
- (7) The provisions contained in sub-section (5) and sub-sections (7) to (12) of section 80-IA shall, so far as may be, apply to the eligible undertaking or enterprise under this section.
- (8) For the purposes of this section,—
 - (i) “Industrial Area” means such areas, which the Board, may, by notification in the Official Gazette, specify in accordance with the scheme framed and notified by the Central Government;
 - (ii) “Industrial Estate” means such estates, which the Board, may, by notification in the Official Gazette, specify in accordance with the scheme framed and notified by the Central Government;
 - (iii) “Industrial Growth Centre” means such centres, which the Board, may, by notification in the Official Gazette, specify in accordance with the scheme framed and notified by the Central Government;
 - (iv) “Industrial Park” means such parks, which the Board, may, by notification in the Official Gazette, specify in accordance with the scheme framed and notified by the Central Government;
 - (v) “Initial assessment year” means the assessment year relevant to the previous year in which the undertaking or the enterprise begins to manufacture or produce articles or things, or commences operation or completes substantial expansion;



- (vi) “Integrated Infrastructure Development Centre” means such centres, which the Board, may, by notification in the Official Gazette, specify in accordance with the scheme framed and notified by the Central Government;
- (vii) “North-Eastern States” means the States of Arunachal Pradesh, Assam, Manipur, Meghalaya, Mizoram, Nagaland and Tripura;
- (viii) “Software Technology Park” means any park set up in accordance with the Software Technology Park Scheme notified by the Government of India in the Ministry of Commerce and Industry;
- (ix) “substantial expansion” means increase in the investment in the plant and machinery by at least fifty per cent 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;
- (x) “Theme Park” means such parks, which the Board, may, by notification in the Official Gazette, specify in accordance with the scheme framed and notified by the Central Government.

Deduction in respect of profits and gains from business of hotels and convention centres in specified area [Sec. 80ID]

- (1) Where the gross total income of an assessee includes any profits and gains derived by an undertaking from any business referred to in sub-section (2) (such business being hereinafter referred to as the eligible business), there shall, in accordance with and subject to the provisions of this section, be allowed, in computing the total income of the assessee, a deduction of an amount equal to hundred per cent of the profits and gains derived from such business for five consecutive assessment years beginning from the initial assessment year.
- (2) This section applies to any undertaking,—
 - (i) engaged in the business of hotel located in the specified area, if such hotel is constructed and has started or starts functioning at any time during the period beginning on the 1st day of April, 2007 and ending on the 31st day of March, 2010; or
 - (ii) engaged in the business of building, owning and operating a convention centre, located in the specified area, if such convention centre is constructed at any time during the period beginning on the 1st day of April, 2007 and ending on the 31st day of March, 2010.
- (3) The deduction under sub-section (1) shall be available only if —
 - (i) the eligible business is not formed by the splitting up, or the reconstruction, of a business already in existence;
 - (ii) the eligible business is not formed by the transfer to a new business of a building previously used as a hotel or a convention centre, as the case may be;
 - (iii) the eligible business is not formed by the transfer to a new business of machinery or plant previously used for any purpose.
 - (iv) the assessee furnishes along with the return of income, the report of an audit in such form and containing such particulars as may be prescribed, and duly signed and verified by an accountant, as defined in the Explanation below sub-section (2) of section 288, certifying that the deduction has been correctly claimed.
- (4) Notwithstanding anything contained in any other provision of this Act, in computing the total income of the assessee, no deduction shall be allowed under any other section contained in Chapter VIA or section 10AA, in relation to the profits and gains of the undertaking.
- (5) The provisions contained in sub-section (5) and sub-sections (8) to (11) of section 80-IA shall, so far as may be, apply to the eligible business under this section.

Special provisions in respect of certain undertakings in North- Eastern States[Sec. 80IE]

- (1) Where the gross total income of an assessee includes any profits and gains derived by an undertaking, to which this section applies, from any business referred to in sub-section (2), there shall be allowed, in computing

the total income of the assessee, a deduction of an amount equal to hundred per cent of the profits and gains derived from such business for ten consecutive assessment years commencing with the initial assessment year.

- (2) This section applies to any undertaking which has, during the period beginning on the 1st day of April, 2007 and ending before the 1st day of April, 2017, begun or begins, in any of the North-Eastern States,—
- (i) to manufacture or produce any eligible article or thing;
 - (ii) to undertake substantial expansion to manufacture or produce any eligible article or thing;
 - (iii) to carry on any eligible business.
- (3) This section applies to any undertaking which fulfils all the following conditions, namely:—
- (i) it is not formed by splitting up, or the reconstruction, of a business already in existence :
Provided that this condition shall not apply in respect of an undertaking which is formed as a result of the re-establishment, reconstruction or revival by the assessee of the business of any such undertaking as referred to in section 33B, in the circumstances and within the period specified in the said section;
 - (ii) it is not formed by the transfer to a new business of machinery or plant previously used for any purpose.

Explanation : The provisions of *Explanations 1* and *2* to sub-section (3) of section 80-IA shall apply for the purposes of clause (ii) of this sub-section as they apply for the purposes of clause (ii) of that sub-section.

- (4) Notwithstanding anything contained in any other provision of this Act, in computing the total income of the assessee, no deduction shall be allowed under any other section contained in Chapter VIA or in section 10A or section 10AA or section 10B or section 10BA, in relation to the profits and gains of the undertaking.
- (5) Notwithstanding anything contained in this Act, no deduction shall be allowed to any undertaking under this section, where the total period of deduction inclusive of the period of deduction under this section, or under section 80-IC or under the second proviso to sub-section (4) of section 80-IB or under section 10C, as the case may be, exceeds ten assessment years.
- (6) The provisions contained in sub-section (5) and sub-sections (7) to (12) of section 80-IA shall, so far as may be, apply to the eligible undertaking under this section.

DEDUCTION IN RESPECT OF PROFITS AND GAINS FROM BUSINESS OF COLLECTING AND PROCESSING OF BIO- DEGRADABLE WASTE. [Sec. 80JJA]

With effect from assessment year 1999-2000, where the gross total income of an assessee include profits and gains derived from the business of collecting and processing or treatment of bio-degradable waste for generating power, or producing bio-fertilizers, bio-pesticides or other biological agents or for producing bio-gas or making patents these shall be allowed in computing the total income of the assessee, a deduction of an amount equal to the whole of such profits and gains for a period of five consecutive assessment years beginning with the assessment year relevant to the previous year in which such business commences.

DEDUCTION IN RESPECT OF EMPLOYMENT OF NEW WORKMEN [Sec 80JJAA]

With effect from assessment year 1999-2000, an Indian company is alongwith for deduction provided the following conditions are satisfied :

- (i) The gross total income of the assessee includes profits and gains derived from any industrial undertaking
- (ii) Such industrial undertaking is engaged in the manufacture or production of article or thing.
- (iii) Such industrial undertaking is not forwarded by (a) splitting up of an existing undertaking, or (b) reconstruction of an existing undertaking or (c) amalgamation with another Industrial undertaking.
- (iv) The assessee employs new regular workmen in the previous year
- (v) The assessee furnishes the report of a chartered accountant in Form No. 10DA [Rule 19AB]

Deduction is available for 3 previous years commencing from the previous year in which such employment is provided.



Amount of deduction

- (i) **New Industrial undertaking** : 30% of the wages paid to regular workmen in excess of 100 regular workmen employed during the year.
- (ii) **Existing undertaking** : 30% of the wages paid to new regular workmen provided there is at least 10% increase in number of regular workmen over the existing member of workmen employed in such undertaking, as on the last day of the preceding year.

Regular workmen

It does not include :—

- (a) a casual workmen or
- (b) a workmen employed through contract labour; or
- (c) any other workman employed for a period of less than 300 days during the previous year.

Deductions in respect of certain incomes of Offshore Banking Units and International Financial Services Centre [Sec. 80LA]

- (1) Where the gross total income of an assessee,—
 - (i) being a scheduled bank, or, any bank incorporated by or under the laws of a country outside India; and having an Offshore Banking Unit in a Special Economic Zone; or
 - (ii) being a Unit of an International Financial Services Centre, includes any income referred to in sub-section (2), there shall be allowed, in accordance with and subject to the provisions of this section, a deduction from such income, of an amount equal to—
 - (a) one hundred per cent of such income for five consecutive assessment years beginning with the assessment year relevant to the previous year in which the permission, under clause (a) of sub-section (1) of section 23 of the Banking Regulation Act, 1949 (10 of 1949) or permission or registration under the Securities and Exchange Board of India Act, 1992 (15 of 1992) or any other relevant law was obtained, and thereafter;
 - (b) fifty per cent of such income for five consecutive assessment years.
- (2) The income referred to in sub-section (1) shall be the income—
 - (a) from an Offshore Banking Unit in a Special Economic Zone; or
 - (b) from the business referred to in sub-section (1) of section 6 of the Banking Regulation Act, 1949 (10 of 1949) with an undertaking located in a Special Economic Zone or any other undertaking which develops, develops and operates or develops, operates and maintains a Special Economic Zone; or
 - (c) from any Unit of the International Financial Services Centre from its business for which it has been approved for setting up in such a Centre in a Special Economic Zone.
- (3) No deduction under this section shall be allowed unless the assessee furnishes along with the return of income,—
 - (i) the report, in the form specified by the Central Board of Direct Taxes under clause (i) of sub-section (2) of section 80LA, as it stood immediately before its substitution by this section, of an accountant as defined in the *Explanation* below sub-section (2) of section 288, certifying that the deduction has been correctly claimed in accordance with the provisions of this section; and
 - (ii) a copy of the permission obtained under clause (a) of sub-section (1) of section 23 of the Banking Regulation Act, 1949 (10 of 1949).

Explanation : For the purposes of this section,—

- (a) “International Financial Services Centre” shall have the same meaning as assigned to it in clause (q) of section 2 of the Special Economic Zones Act, 2005;
- (b) “scheduled bank” shall have the same meaning as assigned to it in clause (e) of section 2 of the Reserve Bank of India Act, 1934 (2 of 1934);
- (c) “Special Economic Zone” shall have the same meaning as assigned to it in clause (za) of section 2 of the Special Economic Zones Act, 2005;

- (d) "Unit" shall have the same meaning as assigned to it in clause (zc) of section 2 of the Special Economic Zones Act, 2005.

DEDUCTION IN RESPECT OF CO-OPERATIVE SOCIETIES [Sec. 80P]

The following amounts are allowed as deduction under this section –

- (i) 100% of the profits attributable to any or more of the following activities in the case of a cooperative society engaged in –
- (a) carrying on business of banking or providing credit facilities to its members; or
 - (b) a cottage industry; or
 - (c) the marketing of the agricultural produce of its members; or
 - (d) the purchase of agricultural implements, seeds, live stock or other articles intended for agriculture for the purpose of supplying them to its members;
 - (e) processing without aid of power of the agricultural produce of its members; or
 - (f) the collective disposal of the labour of its members; or
 - (g) fishing or allied activities; or
 - (h) primary cooperative society engaged in supplying milk raised by its member to a Federal Milk Coop. Society or to the Government or a local authority or a Govt. Company or Corporation established under Central/State or Provincial, Act. Similar benefit is also extended to a primary Cooperative Society engaged in supplying oilseeds, fruits and vegetables raised or grown by its members.
- (ii) The whole of interest and dividend income derived by a Cooperative Society from its investments in any other Cooperative Society;
- (iii) The whole of interest income from securities and property income in the case of a Cooperative Society other than housing society or an urban Consumer Society or a Society carrying on transport business where gross total income does not exceed ₹ 20,000.

Urban Consumer Cooperative Society means a society for the benefit of consumers within the limits of municipal corporation, municipality, municipal committee, notified area committee, town are or cantonment.

- (iv) In respect of other activities carried on either independently or in addition to above activities upto a sum of ₹ 50,000 (₹ 1,00,000 in case of consumer corporation society) – U/s. 80 P (2)(c).

DEDUCTION IN RESPECT OF ROYALTY OF AUTHORS [Sec. 80QOB]

Allowable to : Any resident individual, being an author/joint author, in respect of any income by way of Lump sum consideration or royalty or copyright fees for assignment or grant of any of his Interests in the copyright of any book.

Amount of Deduction: 100% of the royalty income etc. subject to a maximum of ₹ 3,00,000

In case of royalty or copyright fees, not in lump sum consideration, deduction shall be restricted to 15% of the value of books sold during the previous year.

Conditions:

- (1) The assessee shall furnish a certificate in form 10CCD.
- (2) In case of income received from a source outside India, the assessee shall furnish a certificate in form 10H

DEDUCTION IN RESPECT OF ROYALTY ON PATENTS [Sec. 80RRB]

1	Eligible Assessee	Any resident individual
2	Condition	He must be registered under the Patents Act, 1970 on or after 1.4.2003, as the true and first inventor in respect of an invention, including a co-owner of the patent. The deduction is not available to assignees or mortgagees in respect of all or any rights the patent
3	Maximum Cap	100% of such income subject to a maximum ₹ 3,00,000.
4	Special Provisions	(a) a certificate in form 10CCE duly signed by the Controller under Patents Act.(b) a certificate in form 10H, in case of income received from abroad, certifying that the deduction has been correctly claimed in accordance with this section.

Allowable to : Any resident individual, being a patentee, registered under the Patents Act, 1970 on or after 1.4.2003, as the true and first inventor in respect of an invention, including a co-owner of the patent. The deduction is not available to assignees or mortgagees in respect of all or any rights the patent.

Amount of Deduction: 100% of such income subject to a maximum ₹ 3,00,000.

Conditions: The assessee shall furnish along with his return.

- (a) a certificate in form 10CCE duly signed by the Controller under Patents Act.
- (b) a certificate in form 10H, in case of income received from abroad, certifying that the deduction has been correctly claimed in accordance with this section.

DEDUCTION IN RESPECT OF TOTALLY BLIND OR MENTALLY RETARDED OR PHYSICALLY HANDICAPPED PERSON [Sec. 80U]

A resident individual suffering from permanent physical disability or total blindness or partial blindness or mental retardation reducing his capacity substantially for gainful employment is allowed a deduction of ₹ 50,000 or ₹ 1,00,000 in case of severe disability. The extent of blindness or other physical disability has to be certified by a Registered Medical Practitioner of the concerned discipline.

Quantum of deduction under section 80U increased in case of a person with severe disability [Section 80U] (W.e.f. A.Y. 2010-11)

Under the existing provisions of section 80U, deduction is allowed as under :

₹ 50,000 in case of a person with disability.

₹ 1,00,000 in case of a person with severe disability.

The Act has increased the deduction of ₹ 75,000 to ₹ 1,00,000 in case of a person with severe disability. However, the deduction of ₹ 50,000 in case of a person with disability remains unchanged.

Such certificate has to be obtained from a physician, surgeon, etc. working in a Govt. Hospital. For the purpose of Sec. 80U of the Income Tax Act, 1961 any of the following disabilities shall be regarded as a permanent physical disability [Rule 11DD] e.g.:-

- (i) permanent physical disability of more than 50% in one limb; or
- (ii) permanent physical disability of more than 60% in two or more limbs; or
- (iii) permanent deafness with hearing impairment of 71 decibels and above; or
- (iv) permanent and total loss of voice.

PROBLEM ON DEDUCTIONS FROM GROSS TOTAL INCOME

Illustration 1 : Mr. N is employed at a gross salary of ₹ 8,00,000. He gets ₹ 15,000 interest on bank deposit. He has made the following investment/deposit during the year 2010-2012:

	₹
1. Life insurance premium:	
(i) Own life, insured for ₹ 80,000	15,000
(ii) Brother's life, dependent on him	5,000
(iii) Major son, not dependent on him	4,000
2. Contribution to unrecognised provident fund	60,000
3. Contribution to public provident fund	20,000
4. Contribution to ULIP	5,000
5. Repayment of loan to SBI to purchase a residential house: 50% repayment is towards interest.	1,20,000
6. Infrastructure bonds of an Indian public company under Sec. 80C(2)(xix) He has paid education fees for his 3 children:	10,000
A	12,000
B	9,000
C	6,000

Besides, interest of ₹ 1,632 on NSC-VIII, (purchased during the year 2008-2009) has been credited on them during the year 2011-2012.

Compute deduction u/s 80C for the assessment year 2012-2013.

Solution : **Computation of Deduction u/s 80C of Mr. N for the assessment year 2012-2013**

Particulars	₹	₹
Deduction in respect of contribution to approved savings (Sec. 80C) :		
1. Life insurance premium;		
(i) Own life-	15,000	
(ii) Brother's life	—	
(iii) Major son	4,000	
2. Contribution to unrecognised provident fund	—	
3. Contribution to ULIP	5,000	
4. Contribution to public provident fund	20,000	
5. Repayment of housing loan to SBI	60,000	
6. Infrastructure bonds of Indian public company [Sec. 80C(xix)]	10,000	
7. Accrued interest on NSC- VIII issue	1,632	
8. Education fees for two children:		
A	12,000	
B	9,000	
	1,33,632	
Deduction restricted upto ₹ 1,00,000		1,00,000

Illustration 2 : Mr Jamal resident in India, has paid ₹ 60,000 for medical expenses during the previous year 2011-2012 for his wife suffering from cancer. Mrs. Jamal is also resident in India and turns 60 years of age on 31st March 2012. The full treatment cost has been reimbursed by the General Insurance Corporation of India. Please determine if Mr. Jamal is entitled to any deduction under Sec. 80DDB and if the answer is yes, determine the quantum of deduction. Also, please work out the quantum of deduction in the following circumstances :



- I. Mrs. Jamal turns 60 years of age on 1 April 2011 and the amount reimbursed by the insurer is ₹ 25,000. Payment of medical treatment was made out of exempted income.
- II. Jamal turns 60 years of age on 1 April 2011 but Mrs. Jamal is 64 years, 11 months and 30 days as on 31 March 2012 and the insurer has not reimbursed any expenditure.
- III. Mrs. Jamal is 61 years of age, a non-residential in India and the insurer has reimbursed ₹ 35,000
- IV. Mr. Jamal, though having assessable income in India, is actually resident in Sri Lanka and is getting his wife treated in India for sake of better and more advanced medical facilities Mrs. Jamal is residential in India and the insurer has reimbursed ₹ 20,000.
- V. The expenditure is incurred by the assessee on cancer treatment of his 25 year old grandson who is dependent on him and is resident in India. The insurer has not reimbursed the claim.
- VI. Mr. Jamal is able to produce the receipt of the medical expenditure only to the extent of ₹ 10,000 as he misplaced other receipts and the certificate in Form 10-I regarding the treatment of his wife does not mention the total amount incurred by him during the previous year. The insurer has reimbursed only ₹ 5,000.

Solution : Amount of deduction under Sec. 80DDB : PY 2011-2012 / AY 2012-2013

Particulars	Existing	I	II	III	IV	V	VI
Gross deduction u/s 80DDB in respect of specified ailment of dependant wife.	60,000	40,000	40,000	40,000	Nil	Nil	10,000
Less : Insurance claim received	60,000	25,000	Nil	35,000	Nil	Nil	50,000
Net deduction allowable u/s 80DDB	Nil	15,000	40,000	5,000	Nil	Nil	5,000

Working Notes :

1. In order to be a senior citizen, a person should be a resident in India and be 60 years of age at any time during the previous year, be it one the last day of the previous year or at any time during the previous year. Therefore, except when Mrs. Jamal turns 60 after the end of the previous year or when she is a non-resident in India, the gross amount of deduction will be ₹ 40,000.
2. The assessee individual must be resident in India in order to be eligible to the deduction. A grandson is not covered by the definition of "dependant".
3. Form No. 10-I does not require the doctor to certify the amount incurred.

Illustration 3 : Mr. C, manager of L Ltd., has paid ₹ 38,000 during the previous year 2011-2012 by way of medical insurance under GIC approved medical policies. The details are given as below:

- (i) For himself. ₹6,000
- (ii) For Mrs C, a Canadian citizen resident in Toronto and not dependent on him ₹5,000
- (iii) For B, married son living with him and dependent on him ₹3,000
- (iv) For D, minor son resident in Toronto and not dependent on him ₹3,000
- (v) For Mrs B, daughter-in-law, dependent on him ₹5,000
- (vi) For E, a minor grandson dependent on him ₹3,000
- (vii) For K, father, 67 years, resident and dependent on him ₹3,000
- (viii) For M, mother, 66 years, resident in Toronto and dependent on him ₹6,000
- (ix) For Grandfather, dependent on him, 95 years of age and resident in India ₹4,000.

C has earned gross salary of ₹ 2,50,000 during the year and also earns ₹ 95,000 as interest from 7% Capital Investment Bonds, purchased on 31 May 2004. Compute his eligible deduction u/s 80D for the previous year 2011-2012 assuming the following situations:

- I. Premium is paid by cheque from his salary income.
- II. Premium is paid in cash from his salary income. He holds a valid receipt for cash payment.
- III. Premium is paid by cheque out of interest from 7% Capital Investment Bonds, acquired on 31-5-2004.
- IV. Premium is paid in cash out of interest from 7% Capital Investment Bonds, acquired on 1-6-2004.

Solution : **Computation of Deduction for Medical Insurance Premium u/s 80D**

Particulars of Medical Insurance premium paid	I ₹	II ₹	III ₹	IV ₹
For himself	6,000	Nil	Nil	Nil
For Mrs. C, a Canadian citizen resident in Toronto and not dependent on him	3,000	Nil	Nil	Nil
For B, married son living with him and dependent on him	2,000	Nil	Nil	Nil
For D, minor son resident in Toronto and not dependent on him	Nil	Nil	Nil	Nil
For Mrs. B, daughter-in-law, dependent on him	Nil	Nil	Nil	Nil
For E a minor grandson, dependent on him	Nil	Nil	Nil	Nil
For K, father, 67 years, resident, a senior citizen and dependent on him	2,000	Nil	Nil	Nil
For M, mother, 66 years, resident in Toronto -not a senior citizen but dependent on him	6,000	Nil	Nil	Nil
For Grandfather, 95 years of age, dependent on him, resident in India, and senior citizen (not a parent, hence not eligible)	Nil	Nil	Nil	Nil
Eligible premium for Deduction u/s 80 D	19,000	Nil	Nil	Nil

Working Notes :

1. Medical insurance premium on spouse's health is always eligible irrespective of whether the spouse is dependent on the assessee or not. The condition of dependency applies only in case of children and parents.
2. Medical premium on health of grandson, grandparents, daughter-in-law or son in-law are not eligible for deduction u/s 80D.
3. Only the premium on health of dependent father will qualify for relaxation as a senior citizen. Since dependent mother is non-resident and, therefore, outside the purview of being a "senior citizen". However, the premium for health of mother will qualify for the normal limit irrespective of the residential status.
4. Any premium paid in cash or by cheque out of exempted income does not qualify for deduction u/s 80D.

Illustration 4 : Mr. Maity, a resident individual, furnishes the following particulars of his income/ expenditure for the previous year 2011-2012 :

	₹
(i) Gross salary	3,00,000
(ii) Income from house property	1,70,000
(iii) Share of profit from an AOP	25,000
(iv) Long-term capital gain	50,000



He has paid medical insurance on his life, his wife and his dependent children. Total premium paid under GIC approved policies is ₹ 10,000 but a sum of ₹ 1,000 was paid in cash due to a prolonged bank clearing strike. He has spent ₹ 20,000 on the treatment of his brother, a dependant with disability. He has also deposited ₹ 25,000 with a specified company u/s 2(h) of Unit Trust of India (Transfer of Undertaking and Repeal) Act, 2003 for maintenance of his brother.

He has paid the following donations during the year:

Particulars of donations made during the year	₹
• Donation to P.M.'s National Relief Fund	10,000
• Donation to Jamia Milia University	5,000
• Donation to National Cultural Fund, set up by Central Government	5,000
• Donation to Delhi Municipal Corporation for Family Planning	12,000
• Donation to Birla Temple (notified)	
• for repair and renovation of the temple	2,000
• for religious ceremonies, prasad, etc. for the benefit of devotees in general	5,000
• Donation to a temple managed by the Residents Welfare Association for its much needed repair and maintenance. The Association is a non-profit entity registered with the Registrar of Societies.	5,000
• Following donations to Pt. Pyare Lai Charitable Trust recognised by the Commissioner u/s 80G(5)(vi).	
(i) Donation in form of equity shares of blue chip companies: The shares were sold by the Trust at their market value of ₹ 75,000 and used wholly towards its charitable objectives. However, shares were transferred at cost,	25,000
(ii) Donation paid in cash,	5,000
(iii) Donation made by cheque,	7,000
(iv) 50 blankets costing ₹ 100 each.	5,000
• Donation made to Indian Olympic Association 80G(2)(c) paid by a/c payee cheque,	7,500
• Donation for developing low cost homes for slum-dwellers, paid	
(i) Delhi Development Authority, and	3,000
(ii) Delhi Slum-dwellers Rehabilitation Society duly registered with the Registrar,	2,500
• The Rajiv Gandhi Foundation	6,000
• National Children's Fund	3,000

Mr Maity borrowed a sum of ₹ 2,00,000 in 2003 @ 9% interest from Harsh Vardhan Charitable Trust (registered under Sec. 80G) to complete his B.Tech. degree from Nalanda University. In March 2010, he repaid a sum of ₹ 75,000 (including ₹ 20,000 interest) to the said trust.

Compute his total income for the assessment year 2012-2013.

Solution : **Computation of Total Income of Mr. Maity for the Assessment Year 2012-2013**

Particulars	₹	₹
1. Income from salary		3,00,000
2. Income from house property		1,70,000
3. Share of profits from an AOP : Exempt (Sec. 86)		Nil
4. Long-term capital gains		50,000
Gross Total Income		5,20,000
5. Deduction from gross total income :		
(i) Medical insurance premium (Sec. 80D)	9,000	
(ii) Expenditure on medical treatment and deposit for maintenance of a handicapped dependent relative (Sec. 80DD) :	50,000	
(iii) Repayment of interest on loan for higher studies (Sec. 80E) (No deduction is allowed for repayment of principal amount of educational loan w.e.f. A.Y. 2008-2009)	20,000	
	79,000	
(iv) Charitable donations Sec. 80G – [See Note below]	42,500	1,21,500
Total Income		3,89,500

Working Note :

	₹	₹
Gross Total Income		5,20,000
Less : Aggregate of :		
(i) Share of profit in AOP entitled to rebate u/s 86.	Nil	
(ii) Any amount qualifying for deduction from GTI exempt for deduction for donation u/s 80G itself.	79,000	
(iii) Long-term capital gain	50,000	
(iv) Any to a NRI from dividend and interest etc. on foreign currency investment referred to u/s 115A, 115AB, 115AC, 115ACA, 115AD.	Nil	
	1,29,000	1,29,000
Adjusted Gross Total Income		3,91,000

Computation of Deduction for Donations u/s 80G

	₹	₹
A. Donations not subject to qualifying amount, eligible for deduction @ 100% of the amount donated :		
(i) Donation to P.M.'s National Relief Fund	10,000	
(ii) Donation to National Cultural Fund, set up by Central Government	5,000	15,000
B. Donation not subject to qualifying amount, eligible for deduction @ 50% of the amount donated :		
(i) The Rajiv Gandhi Foundation	6,000	
(ii) National Children's Fund	3,000	
Only 50% of the amount of donation available as deduction	9,000	4,500
C. Donation subject to qualifying amount :		
(i) Donation to Delhi Municipal Corporation for Family Planning	12,000	
(ii) Donation made to Indian Olympic Association 80G (2)(C) (available only to a company assessee)	Nil	
(iii) Donation to Jamia Milia University	5,000	
(iv) Donation to Birla Temple (notified) for repair and renovation of the temple.	2,000	
(v) Monetary donation to Pt. Pyare Lal Charitable Trust recognised by the Commissioner u/s 80G (5) (vi).	12,000	
(vi) Donation to Delhi Development Authority	3,000	
Aggregate of donations subject to qualifying amount	34,000	
Qualifying amount :		
Lower of the following :		
(a) 10% of Adjusted Gross Total Income, i.e. 39,100, or		
(b) Aggregate of donations, 34,000		
Whichever is less, is qualifying amount = 34,000		
100% of ₹ 12,000 out of the QA of 34,000	12,000	
50% of the balance of the QA i.e. 50% of (34,000-12,000)	11,000	23,000
Total deduction for donations u/s 80G		42,500

1. Medical Insurance Premium paid in cash is not allowable as a deduction.
2. Donation to a notified temple is allowed only if it is towards its repairs or maintenance and not otherwise.
3. Only donations paid in monetary terms that is, either in cash or by cheque are eligible for deduction. Conversion of donations in kind into cash by the donee or mere possibility of their conversion is immaterial.

Illustration 5 : Mr Jamal, a resident assessee, runs a manufacturing business in Delhi. For the previous year 2011-2012, he disclosed his taxable income as below:

	₹
Business profits	2,55,000
Long-term capital gains	25,000
Short-term capital gain	15,000

He has hired furnished accommodation for his own use and pays ₹ 4,000 p.m. He has paid donation amounting to ₹10,000 to National Defence Fund. He has deposited ₹ 50,000 under a scheme framed by the Life Insurance

Corporation for maintenance of his dependant brother with a disability. The disability is certified by the medical authority. Compute his total income for the assessment year 2012-2013.

Solution : **Computation of total income of Mr Jamal — Assessment Year 2012-2013**

Particulars	₹	₹
Income from business (computed)		2,55,000
Long-term capital gain (computed)		25,000
Short-term capital gain (computed)		15,000
Gross Total Income		2,95,000
Deductions from gross total income:		
(i) Deposit for maintenance of a dependent with disability [Sec. 80DD]:	50,000	
(ii) Charitable donations to National Defence Fund [Sec. 80G]:	10,000	
Amount of Deduction @ 100% of ₹ 10,000		
	<u>60,000</u>	
(iii) Expenditure incurred on rent [Sec. 80GG] [W.N.1]	17,000	77,000
Total income		<u>2,18,000</u>

Workings Note 1:

Particulars	₹	₹
Expenditure incurred on rent [Sec. 80GG]:		
• [Rent paid -10% of ATI], i.e. 48,000 -21,000 = 17,000, or		
• 25% of AGTI, i.e. 25% of 2,10,000 = 52,500, or		
• ₹ 2,000 p.m. = ₹ 24,000		
whichever is less, is to be deducted, i.e. ₹ 17,000		
Adjusted Total Income for Sec. 80GG:		
Gross total income		2,95,000
Less: Aggregate of		
(i) All permissible deduction from GTI except for deduction for u/s 80GG	60,000	
(ii) Any long-term capital gain	<u>25,000</u>	<u>85,000</u>
Adjusted Gross Total Income [AGTI] for Sec. 80GG		<u>2,10,000</u>

Illustration 6 : M, resident in India, furnishes the following particulars of his receipts and outgoings during the previous year 2011-2012.

₹

Receipts:

(i) Income from salary	2,00,000
(ii) Income from house property	3,00,000
(iii) Gross winning from crossword puzzle	3,50,000



Outgoing :

(i) Contribution to LIC annuity plan	15,000
(ii) Medical insurance premium:	
(a) For himself	4,000
(b) His wife, not dependent	3,000
(c) Mother, non-resident, 67 years, dependent	5,000
(d) Nephew, wholly dependent with disability	3,000
(e) Grandson, dependent	2,000
(iii) Expenditure on medical treatment and maintenance of the nephew referred to	30,000
(iv) Medical treatment for grandson, suffering from a disease specified under income-tax rules(v)	50,000
(v) Donation to Gujarat government for family planning	50,000
(vi) Scholarship to a poor but meritorious student	20,000
(vii) Contribution to approved scientific research association	30,000
(viii) Contribution to Delhi Municipal Corporation for sewage scheme for slum-dwellers, approved by National Committee	50,000
(ix) Donation to Political party paid during November 2011	20,000

Compute his total income for the assessment year 2012-2013. Make necessary assumptions and clarify them.

Solution :

Computation of Total Income for AY 2012-2013

Particulars	₹	₹
Income from salary		2,00,000
Income from house property		3,00,000
Gross winnings from crossword puzzle		3,50,000
Gross Total Income		8,50,000
Less: Deductions under Chapter VIA :		
Contribution to LIC annuity plan [Sec. 80CCC]	10,000	
Medical insurance premium [Sec, 80D]		
Self	4,000	
His wife	3,000	
Mother, 67 years old	5,000	
Nephew dependent with disability	x	
Grand son	x	
	12,000	
Maintenance and medical treatment of a dependent with disability [Sec. 80DD]		
Expenditure for medical treatment of grandson [Sec. 80DDB]	Nil	
Donations for scientific research or rural development [Sec. 80-GGA]		
(a) Donation to approved scientific research association	30,000	
(b) Contribution to MCD for slum-dwellers scheme, approved by National Committee	50,000	
Donations to political party [Sec. 80GGC w.e.f. 22.9.2004]	20,000	
Charitable donations [Sec. 80G]		
(a) Scholarship to a poor meritorious student	xxx	
(b) Gujarat government for family planning: 100% of qualifying amount		
1. Actual donation = 50,000, or		
2. 10% of specified GT1 = 37,800		
8,50,000 – (3,50,000 + 10,000 + 12,000 + 30,000 + 50,000 + 20,000)		
= ₹3,78,000		
whichever is less, is QA 37,800= 100% of 37,800	37,800	1,59,800
Total Income		6,90,200

Illustration 7 : SK Industries, a diversified group, discloses profit from the following sources for the previous year 2011-2012 :

	(₹ in lakhs)
(i) Profits from small-scale unit, started in 2002-2003	6.00
(ii) Profit from industrial undertaking 2003-2004, in Vidisha, a B-class industrially backward district.	10.00
(iii) Profit from multiplex theatre, started in 2007-2008	
(a) Delhi	4.00
(b) Allahabad	2.00
(iv) Profits form convention centre, started in 2009-2010	
(a) Delhi	5.00
(b) Allahabad	3.00
(v) Profits from Hill View, a hotel started in 2003-2004 at Manali in Himachal Pradesh. Hotel is approved by prescribed authority	10.00
(vi) Profits from undertakings engaged in refining of mineral oil since 1 January 2005 in Uttar Pradesh, not listed in backward state in Eighth Schedule.	10.00

Compute the total income for the assessment year 2012-2013.

Solution :

Computation of Total Income

Particulars	(₹ lakhs)	(₹ lakhs)
(i) Profits from SSI		6.00
(ii) Profits from undertaking located in industrially backward B-class district		10.00
(iii) Profits from multiplex theatre: (4 + 2) =		6.00
(iv) Profits from convention centre : (5+3) =		3.00
(v) Profits from Hill View Hotel		10.00
(vi) Profits from refining undertaking		10.00
Gross Total Income		50.00
Less : Deduction in respect of profits and gains from certain industrial undertaking, other than infrastructure undertakings (Sec. 80-IB) :		
1. Profits from SSI [Sec. 80-IB (3)] : 25% of ₹ 6 Lakh :	1.50	
2. Profits from undertaking in B-class industrially backward district [Sec. 80-IB (4)] 25% of ₹ 10 lakh	2.50	
3. Profits from multiplex theatre [Sec. 80-IB(7A) 50% of ₹ 2 lakh (No deduction for Delhi)	1.00	
4. Profits from convention centre [Sec. 80-IB(7B)] 50% of ₹ 8 lakh	4.00	
5. Profits from Hill View Hotel [Sec. 80-IB(7)] Allowed only for Indian company	Nil	
6. Profits from refining undertaking [Sec. 80-IB(9)]-100% of profits for 7 assessment years	10.00	19.00
Total Income		31.00



Illustration 8 : Evergreen Construction (P) Ltd. has earned profits during the PY 2011-2012 from construction and sale of flats under three housing projects, developed at Rajarhat, Kolkata, details of which are given below:

(₹ in lakhs)

- | | |
|--|-------|
| (a) Profits from construction and sale of flats, built up on a plot of 1.5 acres,
built up area of the flat 1400 sq feet, located 30 km from Kolkata. | 80.00 |
| (b) Profits from construction and sale of flats, built up on a plot of 1 acre,
built up area 1050 sq feet, located within 25 km from Delhi. | 60.00 |
| (c) Profits from construction and sale of flats, built on a plot of 0.90 acre,
built up area 1000 sq feet, located 35 km from Kolkata. | 40.00 |

The housing projects have been approved by the Kolkata Industrial Development Authority in the year 1 April 2006. Compute its total income for the previous year 2011-2012 relevant for the AY 2012-2013. Would your answer be different in the following cases:

- The housing projects were not approved.
- The housing project is carried out in accordance with a scheme approved by West Bengal Government for redevelopment of buildings in slum areas.
- The company was engaged only in the sale of flats and not developing and building the housing project.

Solution :

Computation of Total Income for the AY 2012-2013

Particulars	(₹ in lakh)	(₹ in lakh)
Profits from Project (a)		80.00
Profits from Project (b)		60.00
Profits from Project (c)		<u>40.00</u>
Less :		180.00
Deductions from profits and gains from certain industrial undertaking other than infrastructure undertaking (Sec. 80-IB):		
(i) Profits from Housing Project (a) are fully deductible as the size of flat not exceeding the prescribed area 1500 sq feet.	80.00	
(ii) Profits from Housing Project (b) not deductible as the area of the flat exceeds the prescribed area of 1000 sq feet.	x	
(iii) Profits from Housing Project (c) not deductible as the size of the Housing plot is less than 1 acre.	x	(-) 80.00
Total income		100.00

Illustration 9 : Mekon Ltd., an Indian company, starts an industrial undertaking on 1 April 2011. During the previous year, it earns profits of ₹ 80 lakh before allowing any deduction for wages. Compute its total income for the previous year 2011-2012 taking into account the following employment schedules of workers:

Date of employment	Number of workers	Status of workers	Rate of wages
1-5-2011	90	Casual	300 p.m.
1-6-2011	20	Regular	4000 p.m.
1-7-2011	10	Regular	4000 p.m.

Computation of total income for the AY 2012-2013

Particulars	₹	₹
Profits before allowing deduction for wages		80,00,000
Less: Wages paid to workers [Sec. 37(1)] :		
(i) 90 × ₹ 3000 × 11	29,70,000	
(ii) 20 × ₹ 4000 × 10	8,00,000	
(iii) 10 × ₹ 4000 × 9	3,60,000	
Business Profits and Gross Total Income		38,70,000
Less: Deduction in respect of employment of new workmen [Sec. 80 JJAA] 30% (₹ .4000 × 10 × 10)		(-) 1,20,000
Total Income		37,50,000

Illustration 10 : Mr. R has developed an improved economical model of a motor cycle and got it patented on 31-3-2011 under the Patent Act, 1970. He allowed Z Ltd. to use his patent rights and licenses has been granted to it under the Patent Act, 1970. He has received royalty of ₹ 8,00,000 during the previous year 2011-2012. However, the royalty in accordance with the terms and conditions of the license settled by the Controllers under the said Act is ₹ 2,80,000. He has incurred ₹ 1,00,000 expenses in developing his invention and getting it patented.

Compute his total income for the assessment year 2012-2013 (i) if he is resident in India, (ii) non-resident India.

Solution :

Computation of Total Income for the Assessment Year 2012-2013

Particulars	(i) ₹	(ii) ₹
Income from other sources	8,00,000	8,00,000
Less : Expenses	1,00,000	1,00,000
Gross Total Income (GTI)		
Less : Deduction for respect of royalty on patent (Sec. 80-RRB)		
Least of the followings:		
(a) Income from royalty 5,00,000; or		
(b) Royalty under the terms of license settled by the Controller 2,80,000;		
(c) Maximum limit ₹ 3,00,000		
Whichever is less, is to be deducted	2,80,000	xxx
Total Income	2,20,000	7,00,000

Illustration 11 : Mr. J is suffering with 60% locomotor disability which is certified by medical authority. He is employed as Technical Supervisor with Air Tel at a salary of ₹ 20,000 p.m.

Particulars	₹
(i) Income from government securities	20,000
(ii) Long-term capital loss	(-) 40,000
(iii) Short-term capital gain (Sec. 111A)	1,00,000
(iv) Insurance commission (gross)	1,00,000
(v) Interest on Saving Fund a/c from bank	10,000



He has incurred the following expenses:

- | | |
|---|--------|
| (i) Medical insurance paid by cheque for his father, resident in India and 70 years | 18,000 |
| (ii) Deposit with LIC for maintenance of father, mainly dependant on him for support and maintenance and suffering from low-vision with a severe disability of 80%, as per certificate of the medical authority | |
| (iii) Rent paid for the year 2011-2012 for accommodation hired by him. | 40,000 |

Compute his total income for the assessment year 2012-2013.

Solution : **Computation of Total Income for the Assessment Year 2012-2013**

Particulars	₹	₹
1. Income from salaries		2,40,000
2. Income from capital gains :		
(a) Short-term capital gains (Sec. 111A)		
(b) Long-term capital loss to be carried forward		1,00,000
3. Income from others sources :		Nil
(a) Interest government securities	20,000	
(b) Interest on savings fund a/c with Bank	10,000	
(c) Insurance commission	1,00,000	1,30,000
Gross Total Income		4,70,000
Less : Deductions under Chapter VIA:		
Medical insurance (Sec. 80D)	18,000	
Deduction in respect of maintenance including medical treatment of a department, a person with severe disability (Sec. 80DD)	1,00,000	
Deduction in case of a person with disability (Sec. 80U) :	50,000	
Deduction u/s 80GG :(Least of the followings)		
(a) (i) Rent paid less 10% of Adjusted Gross Total Income		
40,000-23,300 = 16,700,		
(b) (ii) 25% of 2,33,000 Adjusted Gross Total Income=58,250,		
(iii) 2,000 p.m. × 12 = 24,000	16,700	1,84,700
Whichever is less, is or be deducted		
Total Income		2,85,300

Illustration 12 : Mr. Krishna is a lawyer of Allahabad High Court. He keeps his accounts on cash basis. His Receipts and Payments A/c for the year ending 31-03-2012 is given below :

Dr.

Cr.

Receipts	₹	Payments	₹
Balance b/d	3,820	Purchase of Infrastructure Bonds	20,000
Legal fees	3,45,000	Subscription and membership	4,500
Special commission fees	5,500	Purchase of legal books	17,500
Salary from Law College		Rent	47,500
as part time lecture	87,000	Municipal Tax paid on H. P.	3,000
Exam. Remuneration	1,480	Car expenses	44,000
Interest on Bank Deposit	3,500	Office expenses	38,500
Sale proceeds of residential		Electricity Exps.	4,000
property	3,01,000	Income tax	8,000
Dividend from Co-operative		Gift to daughter	12,000
society	1,000	Domestic expenses	85,000
Dividend received from		Donation to Institutions	
the units of UTI	2,000	approved u/s 80G	12,000
Rent from house property	15,000	Car purchased	3,27,000
		Life Insurance premium	16,000
		Balance c/d	1,26,300
	<u>7,65,300</u>		<u>7,65,300</u>

Following information are available :

1. The Rent and electric expenses are related to a house, of which half portion is used for self residence and remaining half portion is used for office.
2. Car is used only for professional purposes.
3. Outstanding legal fees ₹ 10,000.
4. Rent has been paid for 10 months only.
5. Car was purchased on 25-09-2011. Law books purchased are annual publications out of which books of ₹ 2,000 were purchased on 6-4-2011 and balance on 31-10-2011.
6. The house was purchased in January 1987 for ₹ 50,000 and sold on 1-7-2011.
7. Rent of the property which has been sold was ₹ 5,000 p.m. The property was vacated by the tenant on 30-6-2011.

Compute his Total Income for the assessment year 2012-13.



Solution :

Computation of Total Income of Mr. Sen for the assessment year 2012-13

Particulars	₹	₹
1. <i>Income from salary</i> Salary as a part time lecturer Less: Deduction	87,000 Nil	87,000
2. <i>Income from House Property</i> Annual Rent Less: Vacancy Allowance $\left(\frac{60,000}{12} \times 9\right)$ Gross Annual Value (GAV) Less: M/ Tax paid Net Annual Value (NAV) Less: Standard deduction @ 30% of NAV	60,000 45,000 15,000 3,000 12,000 3,600	8,400
3. <i>Income from Profession</i> Professional Earnings: (i) Legal fees (ii) Special commission Less: Allowable expenses (i) Subscription etc. (ii) 1/2 Rent (Office) (iii) Car expenses (iv) 1/2 electric charges (v) Office expenses (vi) Depreciation on car @ 15% on 3,27,000 (vii) Depreciation on books @ 100% on Annual Publication of ₹ 2,000 = 2,000 @ 50% on Others of 15,500 = 7,750	3,45,000 5,500 3,50,500 4,500 23,750 44,000 7,000 38,500 49,050 2,000 7,750 9,750	1,73,950
4. <i>Capital gains :</i> Sale consideration Less: Indexed cost of acquisition $50,000 \times \frac{785}{140}$	3,01,000 2,80,357	20,643
5. <i>Income from Other Sources :</i> Interest on bank deposit Examiner's fees Dividend from Co-operative Society Dividend from UTI Gross Total Income Less : Deductions (i) 80C - LIP (ii) 80G - Donation @ 50% of ₹ 12,000 (iii) 80CCF - Purchase of Infrastructure Bonds	3,500 1,480 1,000 Exempt 2,95,973 16,000 6,000 20,000	5,980 2,95,973 42,000
Total Income		2,53,973
Total Income (rounded off u/s 288A)		2,53,970

Notes :

1. As the assessee follows the cash system of accounting, amount actually received and payment actually made on account of expenditure, during the year, shall be considered for computing the income. Therefore, any outstanding receipts will not be included in the Total Income. Similarly rent not paid for two months will not be allowed as deduction.
2. The system of accounting does not effect the computation of income from salary, house property and capital gains. Therefore, in this case, rent for three months, though not received (as it has not been shown in the Receipt and Payment Account) shall be taken into account in computing the income under the head house property.
3. Car was purchased and put to use for more than 180 days. Therefore, full depreciation @15% has been claimed.
4. Law books worth ₹ 2,000 were purchased and put to use for more than 180 days and are, therefore, eligible for depreciation @100%. The balance books worth ₹ 15,500 were purchased on 31-10-2011; therefore, 50% of the normal depreciation will be allowed as the books were purchased and put to use for less than 180 days. The total depreciation shall, therefore, be ₹ 2,000 + 50% of ₹15,500 = ₹ 9,750.

Illustration 13 : Dr. Paul is running a Nursing Home with his wife Dr. (Mrs.) Paul as a partnership firm Paul & Co. On the basis of the following particulars, compute the total income of Dr. Paul and Dr. (Mrs.) Paul for the assessment year 2012-13.

- | | |
|--|---------------|
| (A) Particulars of income of the Nursing Home | ₹ |
| (i) Income as per Income and Expenditure Account | 3,20,000 |
| (ii) Firm's tax not provided in the account | 48,000 |
| (iii) Donation to Public Charitable Trust exempt u/s 80G debited in the A/c | 35,000 |
| (B) Particulars of Income of Dr. Paul : | |
| (i) 40% of profit from Nursing Home as per books ₹ 1,28,000 | |
| (ii) Dr. Paul had purchased 500 shares of Laha (P) Ltd. at ₹ 110 each in May 1990. On 14-5-2010 Dr. Paul sold 400 shares at ₹ 300 per share. He invested ₹ 40,000 out of the net sale proceeds in Bonds of RECL in June, 2011. The balance of 200 shares were sold in December, 2011 at ₹ 380 per share. | |
| (iii) Dr. Paul is a Director in Raha (P) Ltd. from which he received director's fees amounting to ₹ 4,000. | |
| (iv) Dr. Paul has obtained a loan of ₹ 50,000 from the said company for renovating the Nursing Home. The balance sheet of Laha (P) Ltd. for the Accounting year, <i>inter alia</i> , disclosed the following particulars. | |
| (a) General Reserve | 40,000 |
| (b) Profit & Loss Account (Cr. Balance) | <u>20,000</u> |
| | <u>60,000</u> |
| (v) Share of income from property belonging to HUF of which Dr. Paul is the Karta amounts to ₹ 30,000. | |
| (C) Particulars of Income of Dr. (Mrs.) Paul : | |
| (i) 60% share of profit from Nursing Home as per books | 1,92,000 |
| (ii) Income from dividend from UTI | 18,000 |
| (iii) Income from house property (as computed under Income-tax Act) | 48,000 |
| (D) Particulars of Income of Master Pritam : | |
| Pritam minor son of Dr. Paul and Dr. (Mrs.) Paul has been admitted to the benefits of partnership in Paul & Co. which is carrying on business as Chemists & Druggists. The said firm has two other partners Soham (brother of Dr. Paul) and Priya [brother of Dr. (Mrs.) Paul]. Pritam's share of profits is determined at ₹ 20,000. | |

Solution :

Computation of Total Income of the Firm

A.Y : 2012-13

Income as per Income and Expenditure Account	₹ 3,20,000
Add : Donation to public charitable trust	35,000
Gross Total Income	3,55,000
Donation to public charitable trust being restricted to 10% of Gross Total Income (3,55,000) i.e. 50% of ₹ 35,500	17,750
Total Income	3,37,250
Total tax <i>plus</i> education cess <i>plus</i> SHEC payable by the firm ₹ 1,40,210.	

Computation of Total Income of Dr. Paul

Particulars	₹	₹
1. His income from the Nursing Home is not taxable. (as tax is already paid by the firm)		Nil
2. Capital Gains		
Sale proceeds : 300 shares of ₹ 400 each	1,20,000	
200 shares of ₹ 380 each	76,000	
	1,96,000	
Less : Indexed cost : $55,000 \times \frac{785}{182}$	2,37,225	
	(-) 41,225	
3. Income from other sources :		
(a) Director's fees	4,000	
(b) Deemed dividends u/s 2(22)(e) for having taken a loan from the company in which the assessee has substantial holding	50,000	54,000
Gross Total Income		54,000
Deduction under Chapter VI A		Nil
Total Income		54,000

Computation of Total income of Dr. (Mrs.) Paul

	₹
1. 60% share from Nursing Home is not taxable (as tax is already paid by the firm)	Nil
2. Income from house property (net).	48,000
3. Income from other sources — dividends from UTI	Exempt
Gross Total Income	48,000
Less : Deduction under Chapter VI A	Nil
Total Income	48,000

Notes :

- Share of profit from the firm accruing to minor is not included in the total income of parent as share of profit to a partner is exempt.
- Long-term capital loss cannot be set off against other income and therefore has to be carried forward.

Illustration 14 : From the following details compute the total income of Mr. X, a resident of Delhi, for the AY 2012-13.

Particulars	₹
(a) Salary including Dearness Allowance	6,30,000
(b) Bonus	57,600
(c) Contribution to a Recognised Provident Fund	36,000
(d) Life Insurance Premium	57,000
(e) Rent paid by the Employer for flat provided to Mr. X	90,000
(f) Cost of Furniture provided by the employer at the aforesaid flat	80,000
(g) Rent recovered from Mr. X by employer	36,000
(h) Bills paid by the employer for gas, electricity and water provided free of cost at the above flat	18,000
(i) Mr. X was provided with Company's car (self-driven) also for personal use, not possible to determine expenditure on personal use and all expenses were borne by the employer.	

Mr. X owns a house. The particulars are :	₹
Rent received (12 months)	72,000
Municipal valuation	48,000
Municipal taxes paid	12,000
Ground rent	2,000
Insurance charges	1,000
Collection charges	3,400
Interest on borrowing used for construction of house (constructed in June 2004)	48,000
Other Information :	
Dividend received from UTI India	14,000
Deposits under National Saving Certificate	20,000

Solution :

Assessee : Mr. X

**Previous Year : 2011-12
Computation of Total Income**

Assessment Year : 2012-13

Particulars	₹	₹
Income under the head Salary		
Salary including Dearness Allowance		6,30,000
Bonus		57,600
Gross Salary before including value of perquisites		6,87,600
Value of Concessional Furnished Accommodation [Rule 3(1)]		
Least of Rent Paid by employer		
[₹ 90,000 or 15% of Salary ₹ 6,87,600]		62,000
10% of Furniture Value		
[₹ 80,000 × 10%]	8,000	
Less : Rent recovered from Mr. X	(36,000)	
Gas, Electricity and Water provided by the employer		18,000
Motor Car provided to the employee for use (assumed capacity upto 1.6 litres)		32,400
([₹ 1,800 p.m. + ₹ 900 p.m. for chauffeur] × 12 Months) as per Rule 3		
Gross Income from Salary		8,00,000



Income from House Property :		
Gross Annual Value u/s 23(1) Higher of Municipal Value ₹ 48,000 or Rent Received ₹ 72,000	72,000	
Less : Municipal Taxes paid	(12,000)	
Net Annual Value	60,000	
Less : Deduction		
Standard deduction @ 30% of Net Annual Value u/s 24(a)	(18,000)	
Interest on borrowed capital u/s 24(b)	(48,000)	(6,000)
Income from Other Sources :		
Income from UTI	14,000	
Exemption u/s 10(35)	(14,000)	Nil
GROSS TOTAL INCOME		7,94,000
Less : Deduction under Chapter VIA - Section 80C		
- Contribution to RPF	36,000	
- LIC Premium	57,000	
- Deposits in NSC	20,000	
	1,13,000	
Deduction u/s 80C restricted to ₹1,00,000 [sec. 80CCE]		(1,00,000)
TOTAL INCOME (Rounded Off u/s 288A)		6,94,000

Illustration 15 : Mr. X, Finance Manager of K Ltd. Mumbai, furnishes the following particulars for the previous year 2011-2012.

	₹
(a) Gross Salary (per month) [Tax deducted from Salary ₹ 1,09,000]	64,000
(b) Valuation of medical facility in a hospital maintained by the Company	7,000
(c) Rent Free Accommodation owned by the Company	
(d) Housing Loan of ₹ 6,00,000 at the interest rate of 5% p.a. (no repayment made during the year, to be repaid within 10 years)	
(e) Gift made by the Company on the occasion of wedding anniversary of X	4,750
(f) A wooden table and 4 Chairs were provided to X at his residence (Dining Table). This was purchased on 1.5.2008 for ₹ 60,000 and sold to X on 1.8.2011 for ₹ 30,000	
(g) Personal purchases through Credit Card provided by the Company amounting to ₹ 20,000 was paid by the Company. No part of the amount was recovered from X.	
(h) A Maruti Esteem Car which was purchased by the Company on 16.7.2007 for ₹ 5,50,000 was sold to the assessee on 14.8.2011 for ₹ 1,30,000.	
(i) Other income received by the assessee during the previous year 2011-2012 are :	₹
Interest on Fixed Deposits with a Company	5,000
Income from specified mutual fund	3,000
Interest on bank deposits of a minor married daughter	3,000
Income from UTI received by his handicapped minor son	1,200
(j) Contribution to LIC towards Premium u/s 80CCC	10,000
(k) Deposit in PPF Account made during the year 2011-2012	75,000
(l) Bonds of ICICI (Tax Savings) eligible for tax deduction	25,000

Compute the Taxable Income of Mr. X and the tax liability for the Asst. Year 2012-2013.

Solution :

Assessee : Mr. X

Previous Year : 2011-12
Computation of Total Income

Assessment Year : 2012-13

Particulars	₹	₹
Income from Salaries :		
Basic Salary (₹ 64,000 × 12)		7,68,000
Add : Value of Perquisites :		
1. Value of Medical Facility in hospital maintained by K Ltd. — Treatment in hospital maintained by Employer — Fully Exempt		Nil
2. Rent Free Accommodation owned by Company — Explanation 1 to Sec. 17(2) 15% of salary = 15% of ₹ 7,68,000 (Population > 25 Lakhs)		1,15,200
3. Housing Loans at concessional rate – Rule 3(7)(i) = ₹ 6,00,000 × (10% – 5%)		30,000
4. Use of Furniture & Fittings upto 1.8.2011 - Rule 3(1)(vii) = 10% × ₹ 60,000 × 4/12		2,000
5. Transfer of Assets - Rule 3(7)(viii) — Dining Table as per WN 1 (a) Motor Car as per WN 1 (b)	12,000 <u>95,280</u>	1,07,280
6. Gifts made by the Company on the occasion of the Wedding Anniversary		Nil
7. Credit Card Purchases taxable as perquisite u/s 17(2)		20,000
Gross Income from Salary		10,42,480
Less : Deduction u/s 16		Nil
Net Income from Salaries		10,42,480
Income from Other Sources :		
Interest on Fixed Deposits with a Company	5,000	
Income from specified mutual fund	3,000	
Less : Exempt u/s 10(35)	(3,000)	
Interest on Bank Deposits of minor married daughter	3,000	
Less : Exempt u/s 10(32)	(1,500)	
Income received by handicapped minor son - not clubbed u/s 64(1A)	<u>Nil</u>	6,500
GROSS TOTAL INCOME		10,48,980
Less : Deduction under Chapter VI-A		
U/s 80CCC – Contribution towards Pension Fund		10,000
U/s 80C – Contribution towards PPF		75,000
U/s 80CCF – Bonds of ICICI (Long term infrastructure bonds)		25,000
TOTAL INCOME		9,38,980
TAX PAYABLE		1,33,694
Add : Education Cess @ 2%		2,674
Add : Secondary and Higher Education Cess @ 1%		1,337
Gross Tax Payable		1,37,705
Less : Tax Deducted at source		1,09,000
Net Tax Liability		28,705



Working Notes :

1. Valuation of Perquisites on transfer of Movable Assets :

(a) Transfer of Assets : Dining Table	(₹)
Purchase Price	60,000
Less : Depreciation till date of Sale (₹ 60,000 × 3 × 10%)	(18,000)
WDV as at date of transfer	42,000
Less : Deduction for collection from Employee	(30,000)
Value of Perquisite	12,000
(b) Motor Car	₹
Cost of Purchase (16.7.2007)	5,50,000
Less : Depreciation @ 20% (16.7.2007 - 15.7.2008)	1,10,000
16.7.2008 WDV	4,40,000
Less : Depreciation for 16.7.2008 - 15.7.2009	88,000
16.7.2009 WDV	3,52,000
Less : Depreciation for 16.7.2009 - 15.7.2010	70,400
16.7.2010 WDV	2,81,600
Less : Depreciation for 16.7.2010 - 15.7.2011	56,320
16.7.2011 WDV	2,25,280
Less : Amount Recovered on Transfer	1,30,000
Value of Perquisite	95,280

2. Gifts received from the employer on the occasion of the wedding anniversary

- (a) Taxable as perquisite u/s 17(2).
- (b) As per Rule 3(7)(vi), value of any gift or voucher or token (other than made in cash) or convertible ; in cash on ceremonial occasion or otherwise shall be taxable if the the aggregate value of Gift during the previous year is ₹ 5,000 or more. Since the value of gifts received is less than ₹ 5,000, it shall be exempt from tax.

Illustration 16 : M, an individual, retired from the services of a Company on 31.10.2011. He joined another employer on 1.11.2011 and was in service till end of March 2012, when he furnishes the following details and information —

1. Salary and Allowances for the period

From First Employer	₹ Per month
Basic Salary	30,000
Dearness Allowance	16,000
Conveyance Allowance	6,000
From Second Employer	₹ Per month
Basic Salary	35,000
Fixed Conveyance Allowance	8,000

2. While he was with the first employer, M contributed 10% of his basic salary to a Provident Fund Account with the Regional Provident Fund Commissioner. He did not become a member of the Provident Fund maintained by the second employer.
3. M was permitted by the second employer to encash 15 days leave he had accumulated during his service and received ₹12,500 from his employer.

4. M had constructed a residential house in Chennai in February 2008 for ₹30 Lakhs. Part of the costs of construction was met by borrowals of ₹ 20 lakhs from the Housing Development Corporation, at interest of 12.5% p.a. The loan was taken on June 2006. The loan outstanding at the beginning of the current year was ₹12,00,000. The rate of interest applicable for the current year was reduced to 9% p.a. due to reduction in rates. [He had also borrowed from some relatives ₹4,00,000 on which interest at 15% p.a. was due.] The property had been let-out soon after completion.
5. In the Assessment Year 2008-09, M was allowed a deduction of ₹50,000 for irrecoverable rents. The annual value decided by the Corporation of Chennai for the property is ₹ 80,000. The property was let-out in the current year to a Company on a rent of ₹20,000 p.m. The half-yearly municipal taxes on the property were fixed by the Corporation of Chennai only in August 2011 at ₹15,000 for every half year from 1.4.2008. M paid the taxes due in September 2011 upto the half-year ending 31.3.2011.
6. M also received from the previous tenant ₹ 40,000 (out of the dues of ₹ 50,000).
7. After retirement from the first employer, M received ₹ 4,50,000 from the Regional Provident Fund Commissioner, money was fully invested by him in the 15% Non-Redeemable Debentures issued by the Indian Oil Corporation interest on these had not come in by the end of March 2012.
8. M received interest of ₹ 60,000 on long-term fixed deposits with Banks, ₹ 25,000 as interest on Post Office Savings Bank Accounts and ₹ 20,000 as income from units.
9. M owns a car which is used for office purposes also and it is found that the entire conveyance allowance from his employer had been fully spent on travel for official purposes.
10. One of the policies of insurance taken by M had matured for payment and ₹ 8,00,000 received by him in June 2011 from the LIC was invested by him, in the name of his 16-year old son, in fixed deposits with companies. Interest received upto 31.3.2012 on these deposits was ₹ 90,000. On one of the continuing policies of insurance, M paid a premium of ₹ 60,000 in the year.

Compute M's total income for the Assessment Year 2012-13.

Solution :

Assessee : Mr. M

**Previous Year : 2011-12
Computation of Total Income**

Assessment Year : 2012-13

	₹	₹	₹
Income under the head Salaries			
From First Employer			
Basic Pay (₹ 30,000 × 7)		2,10,000	
Dearness Allowance (₹ 16,000 × 7)		1,12,000	
Conveyance Allowance (₹ 6000 × 7)	42,000		
Less: Exempt u/s 10(14)	(42,000)	Nil	3,22,000
Amount received from Regional Provident Fund Commissioner 4,50,000			
Less: Exempt u/s 10(12)	(4,50,000)	Nil	
From Second Employer			
Basic Salary (₹ 35,000 × 5)		1,75,000	
Conveyance Allowance (₹ 8,000 × 5)	40,000		
Less: Exempt u/s 10(14) (incurred for official performance of duties)	(40,000)	Nil	
Leave Encashment - Fully taxable while in service		12,500	1,87,500
Gross Income from Salary		5,09,500	

Income from House Property :			
Gross Annual Value u/s. 23(1) — Higher of Municipal Value of ₹80,000 or Actual Rent of ₹ 2,40,000		2,40,000	
Less: Municipal Taxes paid during the year @ ₹ 15,000 for every half year from 1.4.2008 upto 31.3.2011 (Current Year - Not Paid)		<u>(90,000)</u>	
Net Annual Value (NAV)		1,50,000	
Less: Deduction @ 30% of NAV u/s 24(a)		(45,000)	
Interest on Borrowed Capital u/s 24(b)			
Loan from Housing Development Corporation:			
Current Period Interest: ₹12,00,000 × 9%	1,08,000		
Prior Period Interest (Interest upto 31.3.2007) [(₹20,00,000 × 12.5%) + (4,00,000 × 15%)] × 10/12 × 1/5	51,667		
Loan from Relative - Current Period Interest (₹ 4,00,000 × 15%)	<u>60,000</u>	(2,19,667)	
Add: Unrealised Rent recovered (taxable in the year of recovery u/s 25AA)		<u>40,000</u>	(74,667)
Income from Other Sources			
Interest on Long-term Fixed Deposits with Bank		60,000	
Interest on Post Office Savings Bank A/c	25,000		
Less: Exempt u/s 10(15)	(25,000)	Nil	
Income from Units of UTI	20,000		
Less: Exempt u/s. 10(35)	<u>(20,000)</u>	Nil	
LIC Policy matured	8,00,000		
Less: Exempt u/s. 10(1D)	<u>(8,00,000)</u>	Nil	
Interest from Fixed Deposits with Companies in the name of minor son	90,000		
Less: Exemption u/s. 10(32)	<u>(1,500)</u>	88,500	1,48,500
Gross Total Income			5,83,333
Less: Deduction under Chapter VI-A— u/s 80C –LIC Premium		(60,000)	
– RPF – 10% of ₹ 1,40,000		<u>(14,000)</u>	74,000
Total Income			5,09,333
Total Income (Rounded Off u/s 288A)			5,09,330

Assumptions :

1. It is presumed that Mr. M accounts for his interest income on receipt basis.
2. Assumed that there has been no repayment of Housing Loan Principal during the year ending 31.3.2006 for the purpose of calculation of prior period interest.
3. Recognised Provident Fund received on retirement shall not be taxable u/s 10 (assuming conditions are satisfied).

4. **Unrealised Rent recovered** : Since the assessee has been allowed a deduction of ₹ 50,000 from his house property income in earlier years in respect of Unrealised Rent, entire ₹ 40,000 recovered during current year becomes taxable.
5. **Deduction of Interest** u/s 24 shall be allowed even if the amount is borrowed from any person other than the Banks/Financial Institutions in respect of Let Out property.

Illustration 17 : Mr. A, a Senior Citizen, has furnished the following particulars relating to his House Properties —

Particulars	House I — ₹	House II — ₹
Nature of Occupation	Self Occupied	Let-out
Municipal Valuation	60,000	1,20,000
Fair Rent	90,000	1,50,000
Standard Rent	75,000	1,40,000
Actual Rent per month	—	12,000
Municipal Taxes paid	6,000	12,000
Interest on Capital borrowed	90,000	80,000

Loan for both Houses were taken on 1.4.2007. House II remained vacant for 4 months.

Besides the above two house, A has inherited during the year 1988-89 an old house from his grandfather. Due to business commitments, he sold the house immediately for a sum of ₹ 250 Lakhs. The house was purchased in 1962 by his grandfather for a sum of ₹ 2 Lakhs. However, the Fair Market Value as on 1.4.1981 was ₹ 30 Lakhs. With the sale proceeds, A purchased a new house in March 2011 for a sum of ₹ 140 Lakhs and the balance was used in his business.

The other income particulars of Mr. A besides the above are as follows (AY 2012–2013) —

- Business Loss ₹ 12 Lakhs
- Income from Other Sources (Bank Interest) ₹ 1 Lakh
- Investments made during the year PF ₹ 70,000
- ICICI Infrastructure Bond Purchased (u/s 80CCF) ₹ 30,000

Compute Total Income of Mr. A and his Tax Liability for the Assessment Year 2012–2013.

DEDUCTION IN COMPUTING TOTAL INCOME



Solution :

Assessee : Mr. A

**Previous Year : 2011-12
Computation of Total Income**

Assessment Year : 2012-13

Particulars	₹	₹	₹
1. Income from House Property :			
(a) House I : Self Occupied — Annual Value u/s 23(2)	Nil		
Less : Deduction u/s 24(b) = Interest on Housing Loan taken on 1.4.2007 (Note 1)	90,000	(90,000)	
(b) House II : Let-out – (Note 2)		(21,000)	(1,11,200)
2. Profits and Gains of Business or Profession – Loss			(12,00,000)
3. Capital Gains — Sale of Residential House Property — Long Term Asset			
Sale Consideration		2,50,00,000	
Less : Expenses on Transfer		Nil	
Net Consideration		2,50,00,000	
Less : Indexed Cost of Acquisition — Fair Market Value as on 1.4.81 × CII of year of Sale / CII of year of first			
holding ($\text{₹ } 20 \text{ Lakhs} \times \frac{785}{161}$)		97,51,553	
Long Term Capital Gain		1,52,48,447	
Less : Exemption u/s 54 — New House purchased		1,40,00,000	12,48,447
4. Income from Other Sources : Bank Interest			1,00,000
Gross Total Income (assuming this balance is out of Income from other sources only)			37,247
Less : Deduction under Chapter VI-A			
u/s 80C – Deposits in PPF		70,000	
u/s 80 CCF – Investments in Long-term Infrastructure Bonds ₹ 30,000 (restricted upto a maximum of ₹ 20,000)		20,000	
		90,000	
However, i.e. Deduction restricted upto the balance of Gross Total Income			37,247
Total Income			NIL

Notes :

1. Assumed that loss from House Property & Loss from Business are at first adjusted inter-head, against Long Term Capital Gains and then against Income from other sources since it is beneficial to the assessee.
2. Deduction under chapter VIA cannot be done against LTCG.
3. It is assumed that the construction of the house was completed **within 3 years** from the end of the financial year in which the loan was taken.

4. **Annual Value of House Property II** is computed as under —

(i) Municipal Value (MV)	1,20,000
(ii) Fair Rental Value (FRV)	1,50,000
(iii) Higher of MV + FRV	1,50,000
(iv) Standard Rent	1,40,000
(v) Reasonable Expected Rent (RER)	1,40,000
[lower of (iii) + (iv)]	
(vi) Annual Rent @ ₹ 12,000 pm	1,44,000
(vii) Unrealised Rent	Nil
(viii) Actual Rent [(vi) – (vii)]	1,44,000
(ix) Vacancy Allowance $\left[\frac{1,44,000}{12} \times 4 \right]$	48,000
(x) Gross Annual Value [(viii) – (ix)]	96,000
Less : Municipal Tax paid	<u>12,000</u>
Net Annual Value (NAV)	84,000
Less : Standard deduction @ 30% of NAV u/s 24(a)	25,000
Less : Interest on borrowed Capital u/s 24(b)	<u>80,000</u>
Income for House II	<u>(21,200)</u>

Illustration 18 : Mr Ashok a senior citizen, owns a property consisting of two blocks of identical size. The first block is used for business purposes. The other block has been let out from 14.2011 to his cousin for ₹20000 p.m. The cost of construction of each block is ₹ 5 lacs (fully met from bank loan), rate of interest on bank loan is 10% p.a. The construction was completed on 31.3.2011. During the year ended 31.3.2012, he had to pay a penal interest of ₹ 2000 in respect of each block on account of delayed payments to the bank for the borrowings. The normal interest paid by him in respect of each block was ₹ 42,000. Principal repayment for each block was ₹ 23,000. An identical block in the same neighbourhood fetches a rent of ₹25,000 per month. Municipal Tax paid in respect of each block was ₹ 12,000.

The income from business prior to adjustment towards depreciation on any asset is ₹ 2,20,000. He follows Mercantile system of accounting. Depreciation on equipments used for business is ₹ 30,000.

On 23.2.2012, he sold shares of B Ltd., a listed share in BSE for ₹ 2,30,000. The share had been purchased 10 months back for ₹ 1,80,000. Security transaction tax paid may be taken as ₹ 220.

Brought forward business loss of a business discontinued on 12.1.2010 is ₹ 90,000. This loss has been determined in pursuance of a return of income filed in time and the current year is the seventh year.

The following payments were effected by him during the year :

1. LIP of ₹ 20,000 on his life and ₹ 12,000 for his son aged 22, engaged as a software engineer and drawing salary of ₹ 25,000 per month.
2. Medclaim premium of ₹ 6,000 for himself & ₹ 5,000 for above son. The premiums were paid by cheque.

You are required to compute the total income for the assessment year 2012-13 and the tax payable. The various heads of income should be properly shown. Ignore the interest on bank loan for the period prior to 1.4.2011, as the bank had waived it.



Solution :

Computation of Total Income of Mr. Ashok for A.Y. 2012-13.

Particulars	Amount ₹	Amount ₹
(1) Income from house property (Let out)		
Gross Annual Value (being Fair rent)	3,00,000	
Less: Municipal tax	<u>12,000</u>	
Net Annual Value (NAV)	2,88,000	
Less: Deduction:-		
u/s 24(a) Standard Deduction (30% of NAV)	86,400	
u/s 24(b) Interest on loan	<u>42,000</u>	
	<u>1,28,400</u>	1,59,600
(2) Profits and gains of business or profession		
Net profit before depreciation	2,20,000	
Less: Expenditure allowed but not debited in P & L Account		
Depreciation on equipment	30,000	
Depreciation on building i.e. 10% of ₹ 5,00,000	<u>50,000</u>	<u>80,000</u>
Profits and gains of business or profession of current year	1,40,000	
Less: Brought forward losses set off u/s 72	<u>(90,000)</u>	50,000
(3) Capital gains		
Consideration for Transfer	2,30,000	
Less: Cost of acquisition	<u>(1,80,000)</u>	
Short Term Capital Gains		<u>50,000</u>
Gross Total Income		<u>2,59,600</u>
Less: Deduction u/s		
80C: LIC Premium paid	32,000	
Repayment of bank loan	<u>23,000</u>	55,000
80D: Medical insurance premium		<u>6,000</u>
Total Income		<u>1,98,600</u>
Tax payable		Nil

Notes :

1. Penal interest is not allowed u/s 24(b)
2. It has been assumed that interest, municipal tax on property used for business have already being charged while computing "business income before depreciation" i.e. ₹ 2,20,000.
3. STT is not allowed as expenditure on transfer.

Illustration 19. Thomas aged 56 years, took voluntary retirement from State Bank of India on 1st May, 2011 under the Voluntary Retirement Scheme (VRS) and received a sum of ₹ 25 lakh on account of VRS benefits. At the time of his retirement, Thomas was having 47 months of service left and had served the organisation for 18 years 11 months. His last drawn Basic Pay ₹ 60,000, D.A. @ 60% of B/Pay (80% of which forming part of salary). Later, he started a business of plying, hiring and leasing of goods carriages from 1st June, 2011 by acquiring 3 heavy vehicles for ₹ 12 lakh, 2 medium goods vehicle for ₹ 5 lakh and 3 light commercial vehicles for ₹ 6 lakh. Although, he did not maintain regular books of account for his business, the diary maintained by him revealed gross receipts of ₹ 3,12,000 for the financial year ended 31st March, 2012 and he incurred an expenditure of ₹ 1,68,500 on the business towards salaries of drivers, repairs, fuel, etc. Depreciation on vehicle is not included in the said expenditure.

During the financial year 2011-12, he received a sum of ₹ 3,00,000 on account of pension from bank and he contributed a sum of ₹ 65,000 to his PPF account maintained with the said bank in the same year. His PPF account was credited with interest of ₹ 35,000 during the financial year 2011-12. He also purchased long-term infrastructure bonds for ₹

20,000; Repayment of educational loan interest for the year ₹ 50,000. He also paid medical infrastructure premium of ₹ 14,000.

Further, he had two residential properties, one is self occupied and other is let out. During the financial year 2011-12, Thomas was able to let out his property only for 11 months on a monthly rent of ₹ 17,000. The total municipal taxes on the let out property was ₹ 8,000, 50% of which was paid by the tenant and 50% by him. The interest on loan taken for renovation of the self occupied property paid by him during the year was ₹ 34,000. The insurance premium on the house and actual repairs and collection charges paid are ₹ 1,600 and ₹ 18,000 respectively and the entire expenditure is borne by him. During the financial year 2011-12, he was able to recover the unrealized rent of ₹ 33,000 from old tenant who vacated the house during the August, 2009 after spending litigation expenses of ₹ 15,000. During the financial year 2011-12, Thomas suffered short term capital loss on account of sale of shares on various dates amounting to ₹ 8,50,500.

From the aforesaid information, you are required to compute the total income of Thomas for the AY. 2012-13 giving reasons in respect of each and every item and indicate the relief/rebate/deduction which he is entitled to claim.

Solution :

Assessee : Mr. Thomas

Previous Year : 2011-2012

Assessment Year : 2012-2013

Computation of Total Income

	₹	₹
(1) Income from Salary		
Pension Received		3,00,000
<u>Voluntary Compensation</u>		
Actual Amount Received	25,00,000	
Less : Exemption u/s 10(10c)		
Least of the following :		
(i) Actual Amount Received	25,00,000	
(ii) Maximum limit	5,00,000	
(iii) Higher of the following :		
(a) Last Drawn Salary × 3 × No. of Fully completed years of service	47,95,200	
= 88,800 × 3 × 18 = 47,95,200		
(b) Last Drawn Salary × Balance of number of months of service left		
= 88,800 × 47 = 41,73,600		
Last Drawn Salary = B/ Pay + D.A (forming part)		
= ₹ [60,000 + 60% of 80% of 60,000]		
= ₹ [60,000 + 28,800]		
= ₹ 88,800		
	<u>5,00,000</u>	
		20,00,000
(2) Income from House Property		
(a) Self occupied :		
Annual Value	Nil	
(-) Interest on Loan u/s 24(b) ₹ 34,000		
- restricted upto ₹ 30,000	<u>(30,000)</u>	(30,000)



	₹	₹
(b) Let-out House Property		
Gross Annual Value		
(being the Rental Value) = $17,000 \times 12$	2,04,000	
Less : Municipal Tax Paid by the assessee during the year		
= $18,000 \times 50\%$	<u>9,000</u>	
Net Annual Value (NAV)	1,95,000	
Less : Standard deduction @ 30% of NAV u/s 24(a)	58,500	
Less : Interest on loan u/s 24(b)	<u>Nil</u>	
	<u>1,36,500</u>	1,06,500
(3) Income from Business or Profession		
Presumptive Income u/s 44AE		
in the Business of plying, leasing or hiring trucks		
(i) Light goods vehicles = $3 \times 4,500 \times 10 =$	1,35,000	
(ii) Medium goods vehicles = $2 \times 4,500 \times 10 =$	90,000	
(iii) Heavy goods vehicles = $3 \times 5,000 \times 10 =$	<u>1,50,000</u>	3,75,000
(5) Income from Capital Gains		
Short Term Capital Loss		<u>(8,50,000)</u>
Gross Total Income		19,31,500
Less : Deductions under Chapter VIA		
u/s 80 C – Deposits in PPF	65,000	
u/s 80D – Medical Insurance Premium	14,000	
u/s 80E – Interest paid on Education loan	50,000	
u/s 80CCF – Investments in Long-term Infrastructure Bonds	<u>20,000</u>	<u>1,49,000</u>
Total Income		<u>17,82,500</u>
Tax on Total Income of ₹ 17,82,500		3,86,750
(+) E/C @ 2%		7,735
(+) SHEC @ 1%		<u>3,868</u>
Tax Payable		<u>3,98,353</u>
Tax Payable (Rounded off u/s 288B)		3,98,350

Illustration 20 : Mr. Anurag is a Cost Accountant in practice. The Income & Expenditure Account for the year ending March 31, 2012 read as follows :

Expenses	₹	Income	₹
To Employees cost	1,50,000	By Professional earnings	16,00,000
To Travelling & Conveyance	50,000	By Dividend income	
To Administration & Office exp.	4,00,000	– from shares	2,00,000
To Interest	1,50,000	– from equity oriented mutual funds	1,00,000
To Demat charges	10,000		
To Net profit	11,40,000		
Total	19,00,000	Total	19,00,000

Other Information :

- Entire Dividend income is claimed as exempt from taxation by virtue of Section 10(34) and 10(35).
- Anurag claims that no expenditure has been incurred against the dividend income, which is claimed as exempt from tax.
- The value of investment in shares as on the first day and the last day of the previous year is ₹ 7,50,000 and ₹ 9,00,000 respectively.
- The value of investment in units of Mutual Funds as on the first day and the last day of the previous year is ₹ 5,00,000 and 2,00,000 respectively.
- All expenditure including interest expenditure of ₹ 1,50,000 incurred by Anurag are relating to taxable and non taxable Income. Demat charges are directly attributable to exempt income.
- The value of the total assets as appearing in the Balance sheet of the assessee as on the first day and last day of the previous year is ₹ 60,00,000 and ₹80,00,000 respectively.

You are required to compute the taxable income of Anurag for the assessment year 2012-13.

Solution :

Computation of Taxable Income A.Y. 2012-13

Particulars	₹
Income from Profits & Gains of Business or Profession – as per Working Note 1	8,40,000
Income from other sources – as per Working Note 2	Nil
Total	4,40,000
Add : Disallowance u/s 14A – as per Working Note 3	31,804
Taxable Income	4,71,804

Working Note 1 — Profits & Gains of Business or Profession

	₹	₹
Net profit as per Income & Expenditure Account		11,40,000
Less : Income considered under other heads		
– Dividend Income from shares	2,00,000	
– Income from UTI	1,00,000	3,00,000
Taxable Income from Profession		8,40,000

Working Note 2 — Income from other sources

	₹	₹
1. Dividend Income from Shares	2,00,000	
Less : Exemt under sec 10(34)	2,00,000	Nil
2. Income from units in Mutual funds	1,00,000	
Less : Exempt under sec 10(35)	1,00,000	Nil
Taxable income from other sources		Nil

Working Note 3 — Disallowance u/s 14A

	₹
(a) Amount of expenditure directly relating to exempt income (Other than interest) — Demat charges	10,000
(b) Amount of interest incurred by way of expenditure other than those included above $(1,50,000 \times 8,25,000 / 70,00,000)$	17,679
(c) Amount equal to 0.5% of the average value of Investments $(8,25,000 \times 0.5\%)$	4,125
Total amount disallowed u/s 14A (a) + (b) + (c)	31,804

Note :

- Average value of Investment = $(7,50,000 + 9,00,000) / 2 = ₹ 8,25,000$.
- Average value of Total Assets = $(60,00,000 + 80,00,000) / 2 = ₹ 70,00,000$.

Illustration 21 : Mr. Samir submits the following information for the A.Y. 2012-13.

Particulars	₹
Taxable Income from Salary	1,64,000
Income from House property :	
House 1 Income	37,000
House 2 loss	(53,000)
Textile Business (discontinued on 10.10.2011)	(20,000)
Brought forward loss of textile business - A.Y. 2009-10	(80,000)
Chemical Business (discontinued on 15.3.2011)	
– b/f loss of previous year 2009-10	(25,000)
– unabsorbed depreciation of previous year 2009-10	(15,000)
– Bad debts earlier deducted recovered in July '2011	40,000
Leather Business	62,000
Interest on securities held as stock in trade	10,000

Determine the gross total income for the assessment year 2012-13 and also compute the amount of loss that can be carried forward to the subsequent years.

Solution :

Computation of Gross Total Income A.Y. 2012-13

	Particulars	₹	₹
I.	Income from Salary :		1,64,000
II.	Income from House property :		
	House 1 Income	37,000	
	House 2 loss	(53,000)	(26,000)
III.	Profits and Gains of Business or Profession :		
	(i) Textile business loss	(20,000)	
	(iii) Chemical business – Bad debts recovered taxable u/s 41(4) 40,000		
	Less : (i) Set off of brought forward loss of P.Y. 2009-10 u/s. 72 (25,000)	15,000	
		(5,000)	
	(iii) Leather Business Income 62,000		
	(iv) Interest on securities held as stock-in-trade 10,000	72,000	
		67,000	
	Less : B/f. business loss ₹ 80,000 restricted to	67,000	Nil
	Gross Total Income		1,38,000

Note :

1. The unabsorbed loss of ₹ 13,000 (80,000-67,000) of Textile business can be carried forward to A.Y. 2012-13 for setoff u/s. 72, even though the business is discontinued.
2. The unabsorbed depreciation of ₹ 15,000 is eligible for set off against any income other than salary income. Since, Gross total income contains the balance of Income from Salary only, Unabsorbed depreciation cannot be adjusted. Hence, carried forward for adjustment in the subsequent years.



STUDY NOTE - 12

INCOMES WHICH DO NOT FORM PART OF TOTAL INCOME

This Study Note includes

- Various Provisions under the Income Tax Act relating to Incomes which do not form part of total income

12.1 INCOMES NOT INCLUDED IN TOTAL INCOME [Sec. 10]

In computing the total income of a previous year of any person, any income falling within any of the following clauses shall not be included—

- (1) agricultural income;
- (2) any sum received by an individual as a member of a Hindu undivided family, where such sum has been paid out of the income of the family, or, in the case of any impartible estate, where such sum has been paid out of the income of the estate belonging to the family ;

Case Laws:

- (i) *Amount must be received in position as member of HUF* - If a person who is a member of a HUF received an allowance not because he is such a member but wholly apart from that position, the exemption does not apply. It is only if the assessee has received the sum in question by virtue of his position as a member of the undivided family to which he claims to belong, that the application of section 14(1) of the 1922 Act is attracted - *Maharaj Kumar of Vizianagaram*, 2 ITR 186 / *Vijayananda Galapati, Maharaj Kumar of Vizianagaram v. CIT* 9 ITC 73
- (ii) *Member must be entitled to demand partition or maintenance* - Only those members of a HUF can claim exemption who either on partition would be entitled to demand a share or are entitled to maintenance under the Hindu law and who, therefore, might be said to have an interest in the joint income of the family - *Kedar Narain Singh v. CIT* 6 ITR 157
- (2A) in the case of a person being a partner of a firm which is separately assessed as such, his share in the total income of the firm.
- (4) (i) in the case of a non-resident, any income by way of interest on such securities or bonds as the Central Government may, by notification in the Official Gazette, specify in this behalf, including income by way of premium on the redemption of such bonds :

Case Law :

- (i) *Interest on deposit of foreign currency not covered by declaration* - The foreign currency, for which no declarations under section 13 of FEMA had been produced by the respondent-assessee but only exchange vouchers issued by the exchange centres outside the country were produced, even if deposited in the NRE account cannot be said to be moneys standing to the credit of the respondent in the NRE account in accordance with the FEMA and the rules made thereunder and the income by way of interest on such moneys would not be exempt from inclusion in the total income of the respondent under section 10(4)(ii) - *CIT v. Purshottam Khatri* 155 Taxman 399.
- (4B) in the case of an individual, being a citizen of India or a person of Indian origin, who is a non-resident, any income from interest on such savings certificates issued before the 1st day of June, 2002 by the Central Government as that Government may, by notification in the Official Gazette, specify in this behalf :
Provided that the individual has subscribed to such certificates in convertible foreign exchange remitted from a country outside India in accordance with the provisions of the Foreign Exchange Regulation Act, 1973 (46 of 1973), and any rules made thereunder.

Explanation.—For the purposes of this clause,—

- (a) a person shall be deemed to be of Indian origin if he, or either of his parents or any of his grandparents, was born in undivided India ;
- (b) “convertible foreign exchange” means foreign exchange which is for the time being treated by the Reserve Bank of India as convertible foreign exchange for the purposes of the Foreign Exchange Regulation Act, 1973 (46 of 1973), and any rules made thereunder ;
- (5) in the case of an individual, the value of any travel concession or assistance received by, or due to, him,—
 - (a) from his employer for himself and his family, in connection with his proceeding on leave to any place in India ;
 - (b) from his employer or former employer for himself and his family, in connection with his proceeding to any place in India after retirement from service or after the termination of his service,

subject to such conditions as may be prescribed (including conditions as to number of journeys and the amount which shall be exempt per head) having regard to the travel concession or assistance granted to the employees of the Central Government :

Explanation.—For the purposes of this clause, “family”, in relation to an individual, means—

- (i) the spouse and children of the individual ; and
- (ii) the parents, brothers and sisters of the individual or any of them, wholly or mainly dependent on the individual

Case Law :

- (i) *Employer must preserve evidence about correctness of leave travel concession availed by employee* - An employer, discharging his statutory obligation under section 192, is not only required to satisfy himself that payment made by him to his employees in respect of leave travel concession is not taxable, as envisaged under section 10(5), but also has to preserve evidence in relation thereto so as to demonstrate and establish to the satisfaction of officer to whom return prescribed under section 206 has been filed that he has not neglected to discharge his statutory obligation of deducting tax at source - *C.E.S.C. Ltd. v. ITO 134 Taxman 511*.
- (6) in the case of an individual who is not a citizen of India,—
 - (ii) the remuneration received by him as an official, by whatever name called, of an embassy, high commission, legation, commission, consulate or the trade representation of a foreign State, or as a member of the staff of any of these officials, for service in such capacity :

Provided that the remuneration received by him as trade commissioner or other official representative in India of the Government of a foreign State (not holding office as such in an honorary capacity), or as a member of the staff of any of those officials, shall be exempt only if the remuneration of the corresponding officials or, as the case may be, members of the staff, if any, of the Government resident for similar purposes in the country concerned enjoys a similar exemption in that country :

Provided further that such members of the staff are subjects of the country represented and are not engaged in any business or profession or employment in India otherwise than as members of such staff

- (vi) the remuneration received by him as an employee of a foreign enterprise for services rendered by him during his stay in India, provided the following conditions are fulfilled—
 - (a) the foreign enterprise is not engaged in any trade or business in India ;
 - (b) his stay in India does not exceed in the aggregate a period of ninety days in such previous year ; and
 - (c) such remuneration is not liable to be deducted from the income of the employer chargeable under this Act ;
- (viii) any income chargeable under the head “Salaries” received by or due to any such individual being a non-resident as remuneration for services rendered in connection with his employment on a foreign ship where his total stay in India does not exceed in the aggregate a period of ninety days in the previous year ;



- (xi) the remuneration received by him as an employee of the Government of a foreign State during his stay in India in connection with his training in any establishment or office of, or in any undertaking owned by,—
 - (i) the Government ; or
 - (ii) any company in which the entire paid-up share capital is held by the Central Government, or any State Government or Governments, or partly by the Central Government and partly by one or more State Governments ; or
 - (iii) any company which is a subsidiary of a company referred to in item (ii) ; or
 - (iv) any corporation established by or under a Central, State or Provincial Act ; or
 - (v) any society registered under the Societies Registration Act, 1860 (14 of 1860), or under any other corresponding law for the time being in force and wholly financed by the Central Government, or any State Government or State Governments, or partly by the Central Government and partly by one or more State Governments ;
- (6A) where in the case of a foreign company deriving income by way of royalty or fees for technical services received from Government or an Indian concern in pursuance of an agreement made by the foreign company with Government or the Indian concern after the 31st day of March, 1976 [but before the 1st day of June, 2002] and,—
 - (a) where the agreement relates to a matter included in the industrial policy, for the time being in force, of the Government of India, such agreement is in accordance with that policy ; and
 - (b) in any other case, the agreement is approved by the Central Government, the tax on such income is payable, under the terms of the agreement, by Government or the Indian concern to the Central Government, the tax so paid.

Explanation.—For the purposes of this clause ³[and clause (6B)]—

- (a) “fees for technical services” shall have the same meaning as in Explanation 2 to clause (vii) of sub-section (1) of section 9
- (b) “foreign company” shall have the same meaning as in section 80B
- (c) “royalty” shall have the same meaning as in *Explanation 2* to clause (vi) of sub-section (1) of section 9
- (6B) where in the case of a non-resident (not being a company) or of a foreign company deriving income (not being salary, royalty or fees for technical services) from Government or an Indian concern in pursuance of an agreement entered into [before the 1st day of June, 2002] by the Central Government with the Government of a foreign State or an international organisation, the tax on such income is payable by Government or the Indian concern to the Central Government under the terms of that agreement or any other related agreement approved by the Central Government, the tax so paid.
- (6BB) where in the case of the Government of a foreign State or a foreign enterprise deriving income from an Indian company engaged in the business of operation of aircraft, as a consideration of acquiring an aircraft or an aircraft engine (other than payment for providing spares, facilities or services in connection with the operation of leased aircraft) on lease under an agreement entered into after the 31st day of March, 1997 but before the 1st day of April, 1999, or entered into after the 31st day of March, 2007 and approved by the Central Government in this behalf and the tax on such income is payable by such Indian company under the terms of that agreement to the Central Government, the tax so paid.

Explanation.—For the purposes of this clause, the expression “foreign enterprise” means a person who is a non-resident,

- (6C) any income arising to such foreign company, as the Central Government may, by notification¹¹ in the Official Gazette, specify in this behalf, by way of ¹²[royalty or] fees for technical services received in pursuance of an agreement entered into with that Government for providing services in or outside India in projects connected with security of India ;
- (7) any allowances or perquisites paid or allowed as such outside India by the Government to a citizen of India for rendering service outside India ;

- (8) in the case of an individual who is assigned to duties in India in connection with any co-operative technical assistance programmes and projects in accordance with an agreement entered into by the Central Government and the Government of a foreign State (the terms whereof provide for the exemption given by this clause)—
- (a) the remuneration received by him directly or indirectly from the Government of that foreign State for such duties, and
 - (b) any other income of such individual which accrues or arises outside India, and is not deemed to accrue or arise in India, in respect of which such individual is required to pay any income or social security tax to the Government of that foreign State ;
- (8A) in the case of a consultant—
- (a) any remuneration or fee received by him or it, directly or indirectly, out of the funds made available to an international organisation [hereafter referred to in this clause and clause (8B) as the agency] under a technical assistance grant agreement between the agency and the Government of a foreign State ; and
 - (b) any other income which accrues or arises to him or it outside India, and is not deemed to accrue or arise in India, in respect of which such consultant is required to pay any income or social security tax to the Government of the country of his or its origin.

Explanation.—In this clause, “consultant” means—

- (i) any individual, who is either not a citizen of India or, being a citizen of India, is not ordinarily resident in India; or
 - (ii) any other person, being a non-resident, engaged by the agency for rendering technical services in India in connection with any technical assistance programme or project, provided the following conditions are fulfilled, namely :—
 - (1) the technical assistance is in accordance with an agreement entered into by the Central Government and the agency ; and
 - (2) the agreement relating to the engagement of the consultant is approved by the prescribed authority¹⁴ for the purposes of this clause ;
- (8B) in the case of an individual who is assigned to duties in India in connection with any technical assistance programme and project in accordance with an agreement entered into by the Central Government and the agency—
- (a) the remuneration received by him, directly or indirectly, for such duties from any consultant referred to in clause (8A) ; and
 - (b) any other income of such individual which accrues or arises outside India, and is not deemed to accrue or arise in India, in respect of which such individual is required to pay any income or social security tax to the country of his origin, provided the following conditions are fulfilled, namely :—
 - (i) the individual is an employee of the consultant referred to in clause (8A) and is either not a citizen of India or, being a citizen of India, is not ordinarily resident in India ; and
 - (ii) the contract of service of such individual is approved by the prescribed authority before the commencement of his service
- (9) the income of any member of the family of any such individual as is referred to in clause (8) or clause (8A) or, as the case may be, clause (8B) accompanying him to India, which accrues or arises outside India, and is not deemed to accrue or arise in India, in respect of which such member is required to pay any income or social security tax to the Government of that foreign State ¹⁵[or, as the case may be, country of origin of such member.



- (10) (i) any death-cum-retirement gratuity received under the revised Pension Rules of the Central Government or, as the case may be, the Central Civil Services (Pension) Rules, 1972, or under any similar scheme applicable to the members of the civil services of the Union or holders of posts connected with defence or of civil posts under the Union (such members or holders being persons not governed by the said Rules) or to the members of the all-India services or to the members of the civil services of a State or holders of civil posts under a State or to the employees of a local authority or any payment of retiring gratuity received under the Pension Code or Regulations applicable to the members of the defence services ;
- (ii) any gratuity received under the Payment of Gratuity Act, 1972 (39 of 1972), to the extent it does not exceed an amount calculated in accordance with the provisions of sub-sections (2) and (3) of section 4 of that Act ;
- (iii) any other gratuity received by an employee on his retirement or on his becoming incapacitated prior to such retirement or on termination of his employment, or any gratuity received by his widow, children or dependants on his death, to the extent it does not, in either case, exceed one-half month's salary for each year of completed service [calculated on the basis of the average salary for the ten months immediately preceding the month in which any such event occurs, subject to such limit as the Central Government may, by notification in the Official Gazette, specify in this behalf having regard to the limit applicable in this behalf to the employees of that Government.

Case Laws:

- (i) In cases not governed by section 10(10)(i) or 10(10)(ii), section 10(10)(iii) applies which excludes the gratuity amount up to rate of 15 days' wages for every year of completed service subject to a maximum in this regard. Therefore, the prescribed limit of gratuity which is to be excluded under section 10(10) is the same irrespective of whether it is paid under the 1972 Act or any other scheme and, therefore, the limit of 15 days wages for completed services, as prescribed under section 10(10)(iii), is not discriminatory and violative of article 14 - *Gwalior Rayons Staff Association v. UOI* 152 Taxman 520
 - (ii) 'Salary' includes dearness allowance and special allowance - Dearness allowance and special allowance must be treated as 'salary' for computing exemption on gratuity - *Addl. CIT v. P. Krishna Kamat* 99 ITR 74
 - (iii) 'Salary' need not be given a wide meaning - The expression 'salary' found in section 10(10) and 10(10AA) cannot be given a wider meaning than found in clause (h) of Rule 2 of Part A of the Fourth Schedule - *K. Gopalakrishnan v. CBDT* 206 ITR 183/73 Taxman 220.
- (10A) (i) any payment in commutation of pension received under the Civil Pensions (Commutation) Rules of the Central Government or under any similar scheme applicable [to the members of the civil services of the Union or holders of posts connected with defence or of civil posts under the Union (such members or holders being persons not governed by the said Rules) or to the members of the all-India services or to the members of the defence services or to the members of the civil services of a State or holders of civil posts under a State or to the employees of a local authority] or a corporation established by a Central, State or Provincial Act ;
 - (ii) any payment in commutation of pension received under any scheme of any other employer, to the extent it does not exceed—
 - (a) in a case where the employee receives any gratuity, the commuted value of one-third of the pension which he is normally entitled to receive, and
 - (b) in any other case, the commuted value of one-half of such pension, such commuted value being determined having regard to the age of the recipient, the state of his health, the rate of interest and officially recognised tables of mortality ;
 - (iii) any payment in commutation of pension received from a fund under clause (23AAB)

Case Law :

- (i) *Commuted pension* - It cannot be said that entire commuted pension is not taxable; it is taxable subject to the provisions of section 10(10A)(iib) - *CIT v. K.A. Narayan* 124 Taxman 880/254 ITR 683.

- (10AA) (i) any payment received by an employee of the Central Government or a State Government as the cash equivalent of the leave salary in respect of the period of earned leave at his credit at the time of his retirement [whether] on superannuation or otherwise ;
- (ii) any payment of the nature referred to in sub-clause (i) received by an employee, other than an employee of the Central Government or a State Government, in respect of so much of the period of earned leave at his credit at the time of his retirement [whether] on superannuation or otherwise as does not exceed [ten] months, calculated on the basis of the average salary drawn by the employee during the period of ten months immediately preceding his retirement [whether] on superannuation or otherwise, [subject to such limit as the Central Government may, by notification in the Official Gazette, specify in this behalf having regard to the limit applicable in this behalf to the employees of that Government

Provided that where any such payments are received by an employee from more than one employer in the same previous year, the aggregate amount exempt from income-tax under this sub-clause shall not exceed the limit so specified

Provided further that where any such payment or payments was or were received in any one or more earlier previous years also and the whole or any part of the amount of such payment or payments was or were not included in the total income of the assessee of such previous year or years, the amount exempt from income-tax under this sub-clause shall not exceed the limit so specified as reduced by the amount or, as the case may be, the aggregate amount not included in the total income of any such previous year or years.

Explanation.—For the purposes of sub-clause (ii),—

the entitlement to earned leave of an employee shall not exceed thirty days for every year of actual service rendered by him as an employee of the employer from whose service he has retired ;

Case Law:

- (I) *Leave encashment while in service is not exempt* - The words 'or otherwise' in section 10(10AA) must draw the restricted meaning *qua* the immediately preceding word 'superannuation which signifies an employee's severance of relationship with his employer in terms of the contract of employment. Therefore, the words 'or otherwise' will not cover cases where the assessee continues to be under the employment of the same employer and receives leave encashment receipt. Such a receipt will not be exempt from tax - *CIT v. Ram Rattan Lal Verma* 145 Taxman 256 / *CIT v. Vijai Pal Singh* 144 Taxman 504 / *CIT v. Ashok Kumar Dixit* 273 ITR 126.
- (10B) any compensation received by a workman under the Industrial Disputes Act, 1947 (14 of 1947), or under any other Act or Rules, orders or notifications issued thereunder or under any standing orders or under any award, contract of service or otherwise, [at the time of his retrenchment :
Provided that the amount exempt under this clause shall not exceed—
- (i) an amount calculated in accordance with the provisions of clause (b) of section 25F of the Industrial Disputes Act, 1947 (14 of 1947) ; or
- (ii) such amount, not being less than fifty thousand rupees, as the Central Government may, by notification⁵¹ in the Official Gazette, specify in this behalf, whichever is less :

Provided further that the preceding proviso shall not apply in respect of any compensation received by a workman in accordance with any scheme which the Central Government may, having regard to the need for extending special protection to the workmen in the undertaking to which such scheme applies and other relevant circumstances, approve in this behalf

Explanation.—For the purposes of this clause—

- (a) compensation received by a workman at the time of the closing down of the undertaking in which he is employed shall be deemed to be compensation received at the time of his retrenchment ;



- (b) compensation received by a workman, at the time of the transfer (whether by agreement or by operation of law) of the ownership or management of the undertaking in which he is employed from the employer in relation to that undertaking to a new employer, shall be deemed to be compensation received at the time of his retrenchment if—
 - (i) the service of the workman has been interrupted by such transfer ; or
 - (ii) the terms and conditions of service applicable to the workman after such transfer are in any way less favourable to the workman than those applicable to him immediately before the transfer ; or
 - (iii) the new employer is, under the terms of such transfer or otherwise, legally not liable to pay to the workman, in the event of his retrenchment, compensation on the basis that his service has been continuous and has not been interrupted by the transfer ;
 - (c) the expressions “employer” and “workman” shall have the same meanings as in the Industrial Disputes Act, 1947 (14 of 1947)
- (10BB) any payments made under the Bhopal Gas Leak Disaster (Processing of Claims) Act, 1985 (21 of 1985), and any scheme framed thereunder except payment made to any assessee in connection with the Bhopal Gas Leak Disaster to the extent such assessee has been allowed a deduction under this Act on account of any loss or damage caused to him by such disaster ;
- (10BC) *any amount received or receivable from the Central Government or a State Government or a local authority by an individual or his legal heir by way of compensation on account of any disaster, except the amount received or receivable to the extent such individual or his legal heir has been allowed a deduction under this Act on account of any loss or damage caused by such disaster.*

Explanation.—For the purposes of this clause, the expression “disaster” shall have the meaning assigned to it under clause (d) of section 2 of the Disaster Management Act, 2005 (53 of 2005)

- (10C) any amount received [or receivable] by an employee of—
- (i) a public sector company ; or
 - (ii) any other company ; or
 - (iii) an authority established under a Central, State or Provincial Act ; or
 - (iv) a local authority ; or
 - (v) a co-operative society ; or
 - (vi) a University established or incorporated by or under a Central, State or Provincial Act and an institution declared to be a University under section 3 of the University Grants Commission Act, 1956 (3 of 1956) ; or
 - (vii) an Indian Institute of Technology within the meaning of clause (g) of section 3 of the Institutes of Technology Act, 1961 (59 of 1961) ; or
 - (viii) any State Government; or
 - (viii) the Central Government; or
 - (viii) an institution, having importance throughout India or in any State or States, as the Central Government may, by notification in the Official Gazette, specify in this behalf; or
 - (viii) such institute of management as the Central Government may, by notification in the Official Gazette, specify in this behalf,

Double benefit under section 10(10C) and section 89 not allowed (Section 10(10C) and section 89) [W.e.f. A.Y. 2010-11]

Very often, a person receives arrears or advance of salary due to him. Since arrears and advance salary is liable to tax, the total income (including such arrears and advance) is assessed at a rate higher than that at which it would otherwise have been assessed if the total income did not include arrears and advance of salary. In other words, arrears and advance salary result in bracket creeping and higher tax burden. With the view to mitigating this excess burden, the provisions of section 89 of the Income-tax Act provide for backward spread of the arrears and forward spread of the advance.

Under the voluntary retirement scheme, the retiree employee receives lump-sum amount in respect of his balance period of service. Such amount is in the nature of advance salary. Section 10(10C) provides for an exemption of ₹ 5 lakhs in respect of such amount. This exemption is provided to mitigate the hardship on account of bracket creeping as a result of the receipt of the amount in lump sum upon voluntary retirement. However, some taxpayers have claimed both the benefit under section 10(10C) and section 89. The courts have also upheld their claims. To nullify the judgement of Courts, the following changes have been made in this regard:

- (a) Insertion of proviso to section 89: With the view to preventing the claim of double benefit, the Act has inserted a proviso to section 89 to provide that no relief shall be granted in respect of any amount received or receivable by an assessee on his voluntary retirement or termination of his service, in accordance with any scheme or schemes of voluntary retirement or in case of a public sector company referred to in section 10(10C)(i), a scheme of voluntary separation, if an exemption in respect of such voluntary retirement or termination of his service or voluntary separation has been claimed by the assessee under section 10(10C) in respect of such, or any other, assessment year.
- (b) Insertion of third proviso to section 10(10C): Correspondingly, the Act has inserted a third proviso to section 10(10C) to provide that where any relief has been allowed to any assessee under section 89 for any assessment year in respect of any amount received or receivable on his voluntary retirement or termination of service or voluntary separation, no exemption under section 10(10C) shall be allowed to him in relation to such, or any other, assessment year.

Case Law :

- (i) *Provision is not discriminatory* - Under section 10(10C) there is no invidious distinction between public sector employees and private sector employees in the matter of taxation nor is it arbitrary and unintelligible amounting to hostile discrimination - *Shashikant Laxman Kale v. Union of India* 52 Taxman 352/185 ITR 104
- (10CC) in the case of an employee, being an individual deriving income in the nature of a perquisite, not provided for by way of monetary payment, within the meaning of clause (2) of section 17, the tax on such income actually paid by his employer, at the option of the employer, on behalf of such employee, notwithstanding anything contained in section 200 of the Companies Act, 1956 (1 of 1956);
- (10D) any sum received under a life insurance policy, including the sum allocated by way of bonus on such policy, other than—
 - (a) any sum received under sub-section (3) of section 80DD or sub-section (3) of section 80DDA ; or
 - (b) any sum received under a Keyman insurance policy; or
 - (c) any sum received under an insurance policy issued on or after the 1st day of April, 2003 in respect of which the premium payable for any of the years during the term of the policy exceeds twenty per cent of the actual capital sum assured:
- (11) any payment from a provident fund to which the Provident Funds Act, 1925 (19 of 1925), applies or from any other provident fund set up by the Central Government and notified by it in this behalf in the Official Gazette.
- (12) the accumulated balance due and becoming payable to an employee participating in a recognised provident fund, to the extent provided in rule 8 of Part A of the Fourth Schedule ;
- (13) any payment from an approved superannuation fund made—
 - (i) on the death of a beneficiary ; or
 - (ii) 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
 - (iii) by way of refund of contributions on the death of a beneficiary ; or
 - (iv) by way of refund of contributions to an employee on his leaving the service in connection with which the fund is established 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 the commencement of this Act and any interest thereon;



Case Law :

- (i) *Amount received on retirement before specified age is not exempt* - Clause (13) of section 10 exempts only the payments received on retirement at or after a specified age. Payments made on resignation will be exempt only if it is after the specified age. Thus, amount received from superannuation fund on resignation before specified age is not eligible for exemption under section 10(13) - *Yogesh Prabhakar Modak*, 268 ITR 26/138 Taxman 121.
- (13A) any special allowance specifically granted to an assessee by his employer to meet expenditure actually incurred on payment of rent (by whatever name called) in respect of residential accommodation occupied by the assessee, to such extent as may be prescribed having regard to the area or place in which such accommodation is situate and other relevant considerations

Explanation.—For the removal of doubts, it is hereby declared that nothing contained in this clause shall apply in a case where—

- (a) the residential accommodation occupied by the assessee is owned by him ; or
- (b) the assessee has not actually incurred expenditure on payment of rent (by whatever name called) in respect of the residential accommodation occupied by him ;

Case Law :

- (i) Where the assessee was residing in his own house and there was no payment of rent, the provisions of sub-section (13A) of section 10 were not attracted - *CIT v. P.D. Singhania* 156 Taxman 504.
- (14) (i) any such special allowance or benefit, not being in the nature of a perquisite within the meaning of clause (2) of section 17 specifically granted to meet expenses wholly, necessarily and exclusively incurred in the performance of the duties of an office or employment of profit [as may be prescribed], to the extent to which such expenses are actually incurred for that purpose ;
- (ii) any such allowance granted to the assessee either 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 the place where he ordinarily resides, or to compensate him for the increased cost of living, [as may be prescribed and to the extent as may be prescribed] :

Provided that nothing in sub-clause (ii) shall apply to any allowance in the nature of personal allowance granted to the assessee to remunerate or compensate him for performing duties of a special nature relating to his office or employment unless such allowance is related to the place of his posting or residence;
- (15) (i) income by way of interest, premium on redemption or other payment on such securities, bonds, annuity certificates, savings certificates, other certificates issued by the Central Government and deposits as the Central Government may, by notification in the Official Gazette, specify in this behalf, subject to such conditions and limits as may be specified in the said notification ;
- (iib) [in the case of an individual or a Hindu undivided family,] interest on such Capital Investment Bonds as the Central Government may, by notification in the Official Gazette, specify in this behalf

Case Law:

- (i) *Interest on terminal benefits* - Under the Income-tax Act, if any income is liable to be taxed, it is not open for High Court to issue a direction to employer (Government of India)/income-tax department not to levy income-tax on interest earned by assessee (employees) on their retirement/terminal benefits - *R.K. Srivastava v. Union of India* 141 Taxman 84.
- (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 Government of a foreign State or a foreign enterprise

under an agreement, [not being an agreement entered into between the 1st day of April, 1997 and the 31st day of March, 1999,] and] approved by the Central Government in this behalf :

Further nothing contained in this clause shall apply to any such agreement entered into on or after the 1st day of April, 2007.

Case Law:

- (i) *Application for approval of lease agreement* - Rejection of application for approval of agreement by Central Government without a speaking order is not justified - *AFT Trust-Sub1 v. Chairman, CBDT* 192 CTR 406.

- (16) scholarships granted to meet the cost of education;

Case law:

- (i) Scholarship granted by employer to son of employee could not be treated as perquisite but would be exempt under section 10(16) - *CIT v. B.L. Garg* 155 Taxman 189 .

- (17) any income by way of—

- (i) daily allowance received by any person by reason of his membership of Parliament or of any State Legislature or of any Committee thereof;
- (ii) any allowance received by any person by reason of his membership of Parliament under the Members of Parliament (Constituency Allowance) Rules, 1986;
- (iii) any constituency allowance received by any person by reason of his membership of any State Legislature under any Act or rules made by that State Legislature;

- (17A) any payment made, whether in cash or in kind,—

- (i) in pursuance of any award instituted in the public interest by the Central Government or any State Government or instituted by any other body and approved by the Central Government in this behalf; or
- (ii) as a reward by the Central Government or any State Government for such purposes as may be approved by the Central Government in this behalf in the public interest;

- (18) any income by way of—

- (i) pension received by an individual who has been in the service of the Central Government or State Government and has been awarded “Param Vir Chakra” or “Maha Vir Chakra” or “Vir Chakra” or such other gallantry award as the Central Government may, by notification in the Official Gazette, specify in this behalf;
- (ii) family pension received by any member of the family of an individual referred to in sub-clause (i).

Explanation.—For the purposes of this clause, the expression “family” shall have the meaning assigned to it in the Explanation to clause (5);

- (19) family pension received by the widow or children or nominated heirs, as the case may be, 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

- (19A) the annual value of any one palace in the occupation of a Ruler, being a palace, the annual value whereof was exempt from income-tax before the commencement of the Constitution (Twenty-sixth Amendment) Act, 1971, by virtue of the provisions of the Merged States (Taxation Concessions) Order, 1949, or the Part B States (Taxation Concessions) Order, 1950, or, as the case may be, the Jammu and Kashmir (Taxation Concessions) Order, 1958:



Provided that for the assessment year commencing on the 1st day of April, 1972, the annual value of every such palace in the occupation of such Ruler during the relevant previous year shall be exempt from income-tax;

- (20) the income of a local authority which is chargeable under the head “Income from house property”, “Capital gains” or “Income from other sources” or from a trade or business carried on by it which accrues or arises from the supply of a commodity or service [(not being water or electricity) within its own jurisdictional area or from the supply of water or electricity within or outside its own jurisdictional area].

Explanation.—For the purposes of this clause, the expression “local authority” means—

- (i) Panchayat as referred to in clause (d) of article 243 of the Constitution; or
- (ii) Municipality as referred to in clause (e) of article 243P of the Constitution; or
- (iii) Municipal Committee and District Board, legally entitled to, or entrusted by the Government with, the control or management of a Municipal or local fund; or
- (iv) Cantonment Board as defined in section 3 of the Cantonments Act, 1924 (2 of 1924)

Case Laws:

- (i) *State Road Transport Corporation is not a local authority* - A State Transport Corporation is not a ‘local authority’ and is, therefore, not entitled to claim exemption of its income by virtue of section 10(20) calculate - *Calcutta State Transport Corpn. v. CIT* 85 Taxman 402/219 ITR 515
 - (ii) *Forest Corporation* - U.P. State Forest Corporation established for preservation of forest could not be treated as local authority merely because the Act which has created the Corporation has called it a local authority - *CIT v. U.P. Forest Corpn.* 97 Taxman 259/230 ITR 945.
- (21) any income of a scientific research association for the time being approved for the purpose of clause (ii) of sub-section (1) of section 35:

Provided that the scientific research association—

- (a) applies its income, or accumulates it for application, wholly and exclusively to the objects for which it is established, and the provisions of sub-section (2) and sub-section (3) of section 11 shall apply in relation to such accumulation subject to the following modifications, namely :—
 - (i) in sub-section (2),—
 - (1) the words, brackets, letters and figure “referred to in clause (a) or clause (b) of sub-section (1) read with the Explanation to that sub-section” shall be omitted;
 - (2) for the words “to charitable or religious purposes”, the words “for the purposes of scientific research” shall be substituted;
 - (3) the reference to “Assessing Officer” in clause (a) thereof shall be construed as a reference to the “prescribed authority” referred to in clause (ii) of sub-section (1) of section 35;
 - (ii) in sub-section (3), in clause (a), for the words “charitable or religious purposes”, the words “the purposes of scientific research” shall be substituted; and
- (b) does not invest or deposit its funds, other than—
 - (i) any assets held by the scientific research association where such assets form part of the corpus of the fund of the association as on the 1st day of June, 1973;
 - (ii) any assets (being debentures issued by, or on behalf of, any company or corporation), acquired by the scientific research association before the 1st day of March, 1983;
 - (iii) any accretion to the shares, forming part of the corpus of the fund mentioned in sub-clause (i), by way of bonus shares allotted to the scientific research association;

- (iv) voluntary contributions received and maintained in the form of jewellery, furniture or any other article as the Board may, by notification in the Official Gazette, specify, for any period during the previous year otherwise than in any one or more of the forms or modes specified in sub-section (5) of section 11

Provided further that the exemption under this clause shall not be denied in relation to voluntary contribution, other than voluntary contribution in cash or voluntary contribution of the nature referred to in clause (b) of the first proviso to this clause, subject to the condition that such voluntary contribution is not held by the scientific research association, otherwise than in any one or more of the forms or modes specified in sub-section (5) of section 11, after the expiry of one year from the end of the previous year in which such asset is acquired or the 31st day of March, 1992, whichever is later:

Provided also that nothing contained in this clause shall apply in relation to any income of the scientific research association, being profits and gains of business, unless the business is incidental to the attainment of its objectives and separate books of account are maintained by it in respect of such business:

Provided also that where the scientific research association is approved by the Central Government and subsequently that Government is satisfied that—

- (i) the scientific research association has not applied its income in accordance with the provisions contained in clause (a) of the first proviso; or
 - (ii) the scientific research association has not invested or deposited its funds in accordance with the provisions contained in clause (b) of the first proviso; or
 - (iii) the activities of the scientific research association are not genuine; or
 - (iv) the activities of the scientific research association are not being carried out in accordance with all or any of the conditions subject to which such association was approved, it may, at any time after giving a reasonable opportunity of showing cause against the proposed withdrawal to the concerned association, by order, withdraw the approval and forward a copy of the order withdrawing the approval to such association and to the Assessing Officer;
- (22B) any income of such news agency set up in India solely for collection and distribution of news as the Central Government may, by notification in the Official Gazette, specify in this behalf:

Provided that the news agency applies its income or accumulates it for application solely for collection and distribution of news and does not distribute its income in any manner to its members:

Provided further that any notification issued by the Central Government under this clause shall, at any one time, have effect for such assessment year or years, not exceeding three assessment years (including an assessment year or years commencing before the date on which such notification is issued) as may be specified in the notification:

Provided also that where the news agency has been specified, by notification, by the Central Government and subsequently that Government is satisfied that such news agency has not applied or accumulated or distributed its income in accordance with the provisions contained in the first proviso, it may, at any time after giving a reasonable opportunity of showing cause, rescind the notification and forward a copy of the order rescinding the notification to such agency and to the Assessing Officer;

- (23A) any income (other than income chargeable under the head “Income from house property” or any income received for rendering any specific services or income by way of interest or dividends derived from its investments) of an association or institution established in India having as its object the control, supervision, regulation or encouragement of the profession of law, medicine, accountancy, engineering or architecture or such other profession as the Central Government may specify in this behalf, from time to time, by notification in the Official Gazette:

Provided that—

- (i) the association or institution applies its income, or accumulates it for application, solely to the objects for which it is established; and



- (ii) the association or institution is for the time being approved for the purpose of this clause by the Central Government by general or special order:

Provided further that where the association or institution has been approved by the Central Government and subsequently that Government is satisfied that—

- (i) such association or institution has not applied or accumulated its income in accordance with the provisions contained in the first proviso; or
- (ii) the activities of the association or institution are not being carried out in accordance with all or any of the conditions subject to which such association or institution was approved, it may, at any time after giving a reasonable opportunity of showing cause against the proposed withdrawal to the concerned association or institution, by order, withdraw the approval and forward a copy of the order withdrawing the approval to such association or institution and to the Assessing Officer;

(23AA) any income received by any person on behalf of any Regimental Fund or Non-Public Fund established by the armed forces of the Union for the welfare of the past and present members of such forces or their dependants

(23AAA) any income received by any person on behalf of a fund established, for such purposes as may be notified by the Board in the Official Gazette, for the welfare of employees or their dependants and of which fund such employees are members if such fund fulfils the following conditions, namely :—

- (a) the fund—
 - (i) applies its income or accumulates it for application, wholly and exclusively to the objects for which it is established; and
 - (ii) invests its funds and contributions and other sums received by it in the forms or modes specified in sub-section (5) of section 11;
- (b) the fund is approved by the Commissioner in accordance with the rules made in this behalf:

Provided that any such approval shall at any one time have effect for such assessment year or years not exceeding three assessment years as may be specified in the order of approval;

(23AAB) any income of a fund, by whatever name called, set up by the Life Insurance Corporation of India on or after the 1st day of August, 1996 [or any other insurer] under a pension scheme,—

- (i) to which contribution is made by any person for the purpose of receiving pension from such fund;
- (ii) which is approved by the Controller of Insurance [or the Insurance Regulatory and Development Authority established under sub-section (1) of section 3 of the Insurance Regulatory and Development Authority Act, 1999 (41 of 1999), as the case may be

Explanation.—For the purposes of this clause, the expression “Controller of Insurance” shall have the meaning assigned to it in clause (5B) of section 2 of the Insurance Act, 1938 (4 of 1938)

(23B) any income of an institution constituted as a public charitable trust or registered under the Societies Registration Act, 1860 (21 of 1860), or under any law corresponding to that Act in force in any part of India, and existing solely for the development of khadi or village industries or both, and not for purposes of profit, to the extent such income is attributable to the business of production, sale, or marketing, of khadi or products of village industries:

Provided that—

- (i) the institution applies its income, or accumulates it for application, solely for the development of khadi or village industries or both; and
- (ii) the institution is, for the time being, approved for the purpose of this clause by the Khadi and Village Industries Commission:

Provided further that the Commission shall not, at any one time, grant such approval for more than three assessment years beginning with the assessment year next following the financial year in which it is granted:

Provided also that where the institution has been approved by the Khadi and Village Industries Commission and subsequently that Commission is satisfied that—

- (i) the institution has not applied or accumulated its income in accordance with the provisions contained in the first proviso; or
- (ii) the activities of the institution are not being carried out in accordance with all or any of the conditions subject to which such institution was approved, it may, at any time after giving a reasonable opportunity of showing cause against the proposed withdrawal to the concerned institution, by order, withdraw the approval and forward a copy of the order withdrawing the approval to such institution and to the Assessing Officer

Explanation.—For the purposes of this clause,—

- (i) “Khadi and Village Industries Commission” means the Khadi and Village Industries Commission established under the Khadi and Village Industries Commission Act, 1956 (61 of 1956);
- (ii) “khadi” and “village industries” have the meanings respectively assigned to them in that Act

(23BB) any income of an authority (whether known as the Khadi and Village Industries Board or by any other name) established in a State by or under a State or Provincial Act for the development of khadi or village industries in the State.

Explanation.—For the purposes of this clause, “khadi” and “village industries” have the meanings respectively assigned to them in the Khadi and Village Industries Commission Act, 1956 (61 of 1956)

(23BBA) any income of any body or authority (whether or not a body corporate or corporation sole) established, constituted or appointed by or under any Central, State or Provincial Act which provides for the administration of any one or more of the following, that is to say, public religious or charitable trusts or endowments (including maths, temples, gurdwaras, wakfs, churches, synagogues, agiaries or other places of public religious worship) or societies for religious or charitable purposes registered as such under the Societies Registration Act, 1860 (21 of 1860), or any other law for the time being in force:

Provided that nothing in this clause shall be construed to exempt from tax the income of any trust, endowment or society referred to therein;

(23BBB) any income of the European Economic Community derived in India by way of interest, dividends or capital gains from investments made out of its funds under such scheme as the Central Government may, by notification in the Official Gazette, specify in this behalf.

Explanation.—For the purposes of this clause, “European Economic Community” means the European Economic Community established by the Treaty of Rome of 25th March, 1957;

(23BBC) any income of the SAARC Fund for Regional Projects set up by Colombo Declaration issued on the 21st day of December, 1991 by the Heads of State or Government of the Member Countries of South Asian Association for Regional Cooperation established on the 8th day of December, 1985 by the Charter of the South Asian Association for Regional Cooperation

(23BBD) any income of the Secretariat of the Asian Organisation of the Supreme Audit Institutions registered as “ASOSAI-SECRETARIAT” under the Societies Registration Act, 1860 (21 of 1860) for [seven previous years relevant to the assessment years beginning on the 1st day of April, 2001 and ending on the 31st day of March, 2008.

(23BBE) any income of the Insurance Regulatory and Development Authority established under sub-section (1) of section 3 of the Insurance Regulatory and Development Authority Act, 1999 (41 of 1999);



(23BBF) *any income of the North-Eastern Development Finance Corporation Limited, being a company formed and registered under the Companies Act, 1956 (1 of 1956) :*

Provided that in computing the total income of the North-Eastern Development Finance Corporation Limited, the amount to the extent of—

- (i) twenty per cent of the total income for assessment year beginning on the 1st day of April, 2006;
- (ii) forty per cent of the total income for assessment year beginning on the 1st day of April, 2007;
- (iii) sixty per cent of the total income for assessment year beginning on the 1st day of April, 2008;
- (iv) eighty per cent of the total income for assessment year beginning on the 1st day of April, 2009;
- (v) one hundred per cent of the total income for assessment year beginning on the 1st day of April, 2010 and any subsequent assessment year or years, shall be included in such total income;

(23BBG) *any income of the Central Electricity Regulatory Commission constituted under sub-section (1) of section 76 of the Electricity Act, 2003 (36 of 2003);*

(23C) *any income received by any person on behalf of—*

- (i) the Prime Minister's National Relief Fund; or
- (ii) the Prime Minister's Fund (Promotion of Folk Art); or
- (iii) the Prime Minister's Aid to Students Fund; or
- (iiia) the National Foundation for Communal Harmony; or
- (iiiab) any university or other educational institution existing solely for educational purposes and not for purposes of profit, and which is wholly or substantially financed by the Government; or
- (iiiac) any hospital or other institution for the reception and treatment of persons suffering from illness or mental defectiveness or for the reception and treatment of persons during convalescence or of persons requiring medical attention or rehabilitation, existing solely for philanthropic purposes and not for purposes of profit, and which is wholly or substantially financed by the Government; or
- (iiiad) any university or other educational institution existing solely for educational purposes and not for purposes of profit if the aggregate annual receipts of such university or educational institution do not exceed the amount of annual receipts as may be prescribed; or
- (iiiae) any hospital or other institution for the reception and treatment of persons suffering from illness or mental defectiveness or for the reception and treatment of persons during convalescence or of persons requiring medical attention or rehabilitation, existing solely for philanthropic purposes and not for purposes of profit, if the aggregate annual receipts of such hospital or institution do not exceed the amount of annual receipts as may be prescribed or
- (iv) any other fund or institution established for charitable purposes *which may be approved by the prescribed authority*, having regard to the objects of the fund or institution and its importance throughout India or throughout any State or States; or
- (v) any trust (including any other legal obligation) or institution wholly for public religious purposes or wholly for public religious and charitable purposes, *which may be approved by the prescribed authority*, having regard to the manner in which the affairs of the trust or institution are administered and supervised for ensuring that the income accruing thereto is properly applied for the objects thereof;
- (vi) any university or other educational institution existing solely for educational purposes and not for purposes of profit, other than those mentioned in sub-clause (iiiab) or sub-clause (iiiad) and which may be approved by the prescribed authority; or
- (via) any hospital or other institution for the reception and treatment of persons suffering from illness or mental defectiveness or for the reception and treatment of persons during convalescence or of persons

requiring medical attention or rehabilitation, existing solely for philanthropic purposes and not for purposes of profit, other than those mentioned in sub-clause (iii^{ac}) or sub-clause (iii^{ae}) and which may be approved by the prescribed authority

Provided that the fund or trust or institution or any university or other educational institution or any hospital or other medical institution] referred to in sub-clause (iv) or sub-clause (v) or sub-clause (vi) or sub-clause (vi^a) shall make an application in the prescribed form and manner to the prescribed authority for the purpose of grant of the exemption, or continuance thereof, under sub-clause (iv) or sub-clause (v) [or sub-clause (vi) or sub-clause (vi^a)

Provided further that the prescribed authority, before approving any fund or trust or institution or any university or other educational institution or any hospital or other medical institution, under sub-clause (iv) or sub-clause (v) or sub-clause (vi) or sub-clause (vi^a), may call for such documents (including audited annual accounts) or information from the fund or trust or institution or any university or other educational institution or any hospital or other medical institution, as the case may be, as it thinks necessary in order to satisfy itself about the genuineness of the activities of such fund or trust or institution or any university or other educational institution or any hospital or other medical institution, as the case may be, and the prescribed authority may also make such inquiries as it deems necessary in this behalf:

Provided also that the fund or trust or institution [or any university or other educational institution or any hospital or other medical institution] referred to in sub-clause (iv) or sub-clause (v) [or sub-clause (vi) or sub-clause (vi^a)—

- (a) applies its income, or accumulates it for application, wholly and exclusively to the objects for which it is established and in a case where more than fifteen per cent of its income is accumulated on or after the 1st day of April, 2002, the period of the accumulation of the amount exceeding fifteen per cent of its income shall in no case exceed five years; and
- (b) does not invest or deposit its funds, other than—
 - (i) any assets held by the fund, trust or institution or any university or other educational institution or any hospital or other medical institution] where such assets form part of the corpus of the fund, trust or institution or any university or other educational institution or any hospital or other medical institution as on the 1st day of June, 1973;
 - (i^a) any asset, being equity shares of a public company, held by any university or other educational institution or any hospital or other medical institution where such assets form part of the corpus of any university or other educational institution or any hospital or other medical institution as on the 1st day of June, 1998;
 - (ii) any assets (being debentures issued by, or on behalf of, any company or corporation), acquired by the fund, trust or institution or any university or other educational institution or any hospital or other medical institution] before the 1st day of March, 1983;
 - (iii) any accretion to the shares, forming part of the corpus mentioned in sub-clause (i) and sub-clause (i^a), by way of bonus shares allotted to the fund, trust or institution or any university or other educational institution or any hospital or other medical institution
 - (iv) voluntary contributions received and maintained in the form of jewellery, furniture or any other article as the Board may, by notification in the Official Gazette, specify, for any period during the previous year otherwise than in any one or more of the forms or modes specified in sub-section (5) of section 11

Provided also that the exemption under sub-clause (iv) or sub-clause (v) shall not be denied in relation to any funds invested or deposited before the 1st day of April, 1989, otherwise than in any one or more of the forms or modes specified in sub-section (5) of section 11 if such funds do not continue to remain so invested or deposited after the 30th day of March, [1993]

Provided also that the exemption under sub-clause (vi) or sub-clause (vi^a) shall not be denied in relation to any funds invested or deposited before the 1st day of June, 1998, otherwise than in any one or more of the forms or modes specified in sub-section (5) of section 11 if such funds do not continue to remain so invested or deposited after the 30th day of March, 2001

Provided also that the exemption under sub-clause (iv) or sub-clause (v) [or sub-clause (vi) or sub-clause (vi^a)] shall not be denied in relation to voluntary contribution, other than voluntary contribution in cash or voluntary contribution



of the nature referred to in clause (b) of the third proviso to this sub-clause, subject to the condition that such voluntary contribution is not held by the trust or institution or any university or other educational institution or any hospital or other medical institution], otherwise than in any one or more of the forms or modes specified in sub-section (5) of section 11, after the expiry of one year from the end of the previous year in which such asset is acquired or the 31st day of March, 1992, whichever is later

Provided also that nothing contained in sub-clause (iv) or sub-clause (v) or sub-clause (vi) or sub-clause (via)] shall apply in relation to any income of the fund or trust or institution or any university or other educational institution or any hospital or other medical institution], being profits and gains of business, unless the business is incidental to the attainment of its objectives and separate books of account are maintained by it in respect of such business:

Provided also that where the total income, of the fund or trust or institution or any university or other educational institution or any hospital or other medical institution referred to in sub-clause (iv) or sub-clause (v) or sub-clause (vi) or sub-clause (via), without giving effect to the provisions of the said sub-clauses, exceeds the maximum amount which is not chargeable to tax in any previous year, such trust or institution or any university or other educational institution or any hospital or other medical institution shall get its accounts audited in respect of that year by an accountant as defined in the Explanation below sub-section (2) of section 288 and furnish along with the return of income for the relevant assessment year, the report of such audit in the prescribed form duly signed and verified by such accountant and setting forth such particulars as may be prescribed:

Provided also that any amount of donation received by the fund or institution in terms of clause (d) of sub-section (2) of section 80G [in respect of which accounts of income and expenditure have not been rendered to the authority prescribed under clause (v) of sub-section (5C) of that section, in the manner specified in that clause, or] which has been utilised for purposes other than providing relief to the victims of earthquake in Gujarat or which remains unutilised in terms of sub-section (5C) of section 80G and not transferred to the Prime Minister's National Relief Fund on or before the 31st day of March, [2004] shall be deemed to be the income of the previous year and shall accordingly be charged to tax:

Provided also that where the fund or trust or institution or any university or other educational institution or any hospital or other medical institution referred to in sub-clause (iv) or sub-clause (v) or sub-clause (vi) or sub-clause (via) does not apply its income during the year of receipt and accumulates it, any payment or credit out of such accumulation to any trust or institution registered under section 12AA or to any fund or trust or institution or any university or other educational institution or any hospital or other medical institution referred to in sub-clause (iv) or sub-clause (v) or sub-clause (vi) or sub-clause (via) shall not be treated as application of income to the objects for which such fund or trust or institution or university or educational institution or hospital or other medical institution, as the case may be, is established :

Provided also that where the fund or institution referred to in sub-clause (iv) or trust or institution referred to in sub-clause (v) is notified by the Central Government or any university or other educational institution referred to in sub-clause (vi) or any hospital or other medical institution referred to in sub-clause (via), is approved by the prescribed authority and subsequently that Government or the prescribed authority is satisfied that—

- (i) such fund or institution or trust or any university or other educational institution or any hospital or other medical institution has not—
 - (A) applied its income in accordance with the provisions contained in clause (a) of the third proviso; or
 - (B) invested or deposited its funds in accordance with the provisions contained in clause (b) of the third proviso; or
- (ii) the activities of such fund or institution or trust or any university or other educational institution or any hospital or other medical institution—
 - (A) are not genuine; or
 - (B) are not being carried out in accordance with all or any of the conditions subject to which it was notified or approved :

it may, at any time after giving a reasonable opportunity of showing cause against the proposed action to the concerned fund or institution or trust or any university or other educational institution or any hospital or other

medical institution, rescind the notification or, by order, withdraw the approval, as the case may be, and forward a copy of the order rescinding the notification or withdrawing the approval to such fund or institution or trust or any university or other educational institution or any hospital or other medical institution and to the Assessing Officer;

Provided also that in case the fund or trust or institution or any university or other educational institution or any hospital or other medical institution referred to in the first proviso makes an application on or after the 1st day of June, 2006 for the purposes of grant of exemption or continuance thereof, such application shall be made at any time during the financial year immediately preceding the assessment year from which the exemption is sought :

Provided also that any anonymous donation referred to in section 115BBC on which tax is payable in accordance with the provisions of the said section shall be included in the total income

Provided also that all pending applications, on which no notification has been issued under sub-clause (iv) or sub-clause (v) before the 1st day of June, 2007, shall stand transferred on that day to the prescribed authority and the prescribed authority may proceed with such applications under those sub-clauses from the stage at which they were on that day;

Extension of time limit to 30th September for filing application for approval under section 10(23C) for fund or trust or institution or any university or other educational institution or any hospital or other medical institution [Section 10(23C)] [For the financial year 2008-09 and subsequent years]

Section 10(23C) stipulates that income of institutions specified under its various sub-clauses (fund or trust or institution or any university or other educational institution or any hospital or other medical institution) shall be exempt from income tax. For trusts or institutions covered under section 10(23C)(/v), (v), (v/) and (via), approvals are required to be taken from prescribed authorities, in the prescribed manner, to become eligible for claiming exemption. Under the existing provisions, any institution (having receipts of more than rupees one crore) has to make an application for seeking exemption at any time during the financial year for which the exemption is sought. In practice, an eligible institution has to anticipate its annual receipts in order to decide whether the application for exemption is required to be filed or not. This has often led to avoidable hardship.

In order to mitigate this hardship the Act has extended the time limit for filing such application to the 10th day of September in the succeeding financial year. This relaxation has been provided for the financial year 2008-09 and subsequent years. In other words, where the gross receipts of a trust or institution exceeds rupees one crore in the financial year 2008-2009, it can file the application for exemption up till 30th September 2009.

(23D) subject to the provisions of Chapter XII-E, any income of

- (i) a Mutual Fund registered under the Securities and Exchange Board of India Act, 1992 (15 of 1992) or regulations made thereunder;
- (ii) such other Mutual Fund set up by a public sector bank or a public financial institution or authorised by the Reserve Bank of India and subject to such conditions as the Central Government may, by notification in the Official Gazette, specify in this behalf

Explanation.—For the purposes of this clause,—

- (a) the expression “public sector bank” means the State Bank of India constituted under the State Bank of India Act, 1955 (23 of 1955), a subsidiary bank as defined in the State Bank of India (Subsidiary Banks) Act, 1959 (38 of 1959), a corresponding new Bank constituted under section 3 of the Banking Companies (Acquisition and Transfer of Undertakings) Act, 1970 (5 of 1970), or under section 3 of the Banking Companies (Acquisition and Transfer of Undertakings) Act, 1980 (40 of 1980);
- (b) the expression “public financial institution” shall have the meaning assigned to it in section 4A of the Companies Act, 1956 (1 of 1956)
- (c) the expression “Securities and Exchange Board of India” shall have the meaning assigned to it in clause (a) of sub-section (1) of section 2 of the Securities and Exchange Board of India Act, 1992 (15 of 1992);



Amendment to section 10(23) of the Income Tax Act, 1961- Incorporating “Other Public Sector Banks” under the expression “Public Sector Bank” [Section 10(23D)] [W.e.f.A.Y.2010-11]

Income of a mutual fund set up by a Public Sector Bank is exempt under section 10(23D). The expression “public sector banks” has been defined in the Explanation to section 10(23D). Reserve Bank of India has categorized a new sub-group called “other public sector banks”. The Central Government holds more than 51% shareholding in IDBI Bank Limited, which has been categorized under “other public sector banks” by RBI.

Since “other public sector banks”, has not been included in the expression “public sector banks” as defined in the Explanation to section 10(23D), the Act has amended the relevant provisions of the Income-tax Act, 1961 to do so. Hence, income of a mutual fund set up by other public sector banks shall also be exempt.

(23EA) any income [*by way of contributions received from recognised stock exchanges and the members thereof,*] of such Investor Protection Fund set up by recognised stock exchanges in India, either jointly or separately, as the Central Government may, by notification in the Official Gazette, specify in this behalf:

Provided that where any amount standing to the credit of the Fund and not charged to income-tax during any previous year is shared, either wholly or in part, with a recognised stock exchange, the whole of the amount so shared shall be deemed to be the income of the previous year in which such amount is so shared and shall accordingly be chargeable to income-tax;

(23EB) any income of the Credit Guarantee Fund Trust for Small Industries, being a trust created by the Government of India and the Small Industries Development Bank of India established under sub-section (1) of section 3 of the Small Industries Development Bank of India Act, 1989 (39 of 1989), for five previous years relevant to the assessment years beginning on the 1st day of April, 2002 and ending on the 31st day of March, 2007

(23EC) *any income, by way of contributions received from commodity exchanges and the members thereof, of such Investor Protection Fund set up by commodity exchanges in India, either jointly or separately, as the Central Government may, by notification in the Official Gazette, specify in this behalf:*

(23F) any income by way of dividends or long-term capital gains of a venture capital fund or a venture capital company from investments made by way of equity shares in a venture capital undertaking :

Provided that such venture capital fund or venture capital company is approved for the purposes of this clause by the prescribed authority in accordance with the rules made in this behalf and satisfies the prescribed conditions :

Provided further that any approval by the prescribed authority shall, at any one time, have effect for such assessment year or years, not exceeding three assessment years, as may be specified in the order of approval :

Provided also that nothing contained in this clause shall apply in respect of any investment made after the 31st day of March, 1999.

Explanation.—For the purposes of this clause,—

- (a) “venture capital fund” means such fund, operating under a trust deed registered under the provisions of the Registration Act, 1908 (16 of 1908), established to raise monies by the trustees for investments mainly by way of acquiring equity shares of a venture capital undertaking in accordance with the prescribed guidelines;
- (b) “venture capital company” means such company as has made investments by way of acquiring equity shares of venture capital undertakings in accordance with the prescribed guidelines; and
- (c) “venture capital undertaking” means such domestic company whose shares are not listed in a recognised stock exchange in India and which is engaged in the business of generation or generation and distribution of electricity or any other form of power or engaged in the business of providing telecommunication services or in the business of developing, maintaining and operating any infrastructure facility or engaged in the manufacture or production of such articles or things (including computer software) as may be notified by the Central Government in this behalf;

- (d) “infrastructure facility” means a road, highway, bridge, airport, port, rail system, a water supply project, irrigation project, sanitation and sewerage system or any other public facility of a similar nature as may be notified by the Board in this behalf in the Official Gazette and which fulfils the conditions specified in sub-section (4A) of section 80-IA;
- (23FA) any income by way of dividends [, other than dividends referred to in section 115-O], or long-term capital gains of a venture capital fund or a venture capital company from investments made by way of equity shares in a venture capital undertaking :

Provided that such venture capital fund or venture capital company is approved, for the purposes of this clause, by the Central Government on an application made to it in accordance with the rules made in this behalf and which satisfies the prescribed conditions :

Provided further that any approval by the Central Government shall, at any one time, have effect for such assessment year or years, not exceeding three assessment years, as may be specified in the order of approval :

Explanation.—For the purposes of this clause,—

- (a) “venture capital fund” means such fund, operating under a trust deed registered under the provisions of the Registration Act, 1908 (16 of 1908), established to raise monies by the trustees for investments mainly by way of acquiring equity shares of a venture capital undertaking in accordance with the prescribed guidelines;
- (b) “venture capital company” means such company as has made investments by way of acquiring equity shares of venture capital undertakings in accordance with the prescribed guidelines; and
- (c) “venture capital undertaking” means such domestic company whose shares are not listed in a recognised stock exchange in India and which is engaged in the—
- (i) business of—
 - (A) software;
 - (B) information technology;
 - (C) production of basic drugs in the pharmaceutical sector;
 - (D) bio-technology;
 - (E) agriculture and allied sectors; or
 - (F) such other sectors as may be notified by the Central Government in this behalf; or
 - (ii) production or manufacture of any article or substance for which patent has been granted to the National Research Laboratory or any other scientific research institution approved by the Department of Science and Technology;

(23FB) any income of a venture capital company or venture capital fund *set up to raise funds for investment* in a venture capital undertaking.

Explanation [1].—For the purposes of this clause,—

- (a) “venture capital company” means such company—
- (i) which has been granted a certificate of registration under the Securities and Exchange Board of India Act, 1992 (15 of 1992), and regulations made thereunder;
 - (ii) which fulfils the conditions as may be specified, with the approval of the Central Government, by the Securities and Exchange Board of India, by notification in the Official Gazette, in this behalf;



- (b) “venture capital fund” means such fund—
- (i) operating under a trust deed registered under the provisions of the Registration Act, 1908 (16 of 1908) or operating as a venture capital scheme made by the Unit Trust of India established under the Unit Trust of India Act, 1963 (52 of 1963);
 - (ii) which has been granted a certificate of registration under the Securities and Exchange Board of India Act, 1992 (15 of 1992), and regulations made thereunder;
 - (iii) which fulfils the conditions as may be specified, with the approval of the Central Government, by the Securities and Exchange Board of India, by notification in the Official Gazette, in this behalf; and
- (c) “venture capital undertaking” means a venture capital undertaking referred to in the Securities and Exchange Board of India (Venture Capital Funds) Regulations, 1996 made under the Securities and Exchange Board of India Act, 1992 (15 of 1992) and notified as such in the Official Gazette by the Board for the purposes of this clause;]]
- (c) “venture capital undertaking” means such domestic company whose shares are not listed in a recognised stock exchange in India and which is engaged in the—
- (i) *business of—*
 - (A) *nanotechnology;*
 - (B) *information technology relating to hardware and software development;*
 - (C) *seed research and development;*
 - (D) *bio-technology;*
 - (E) *research and development of new chemical entities in the pharmaceutical sector;*
 - (F) *production of bio-fuels;*
 - (G) *building and operating composite hotel-cum-convention centre with seating capacity of more than three thousand;*
or
 - (H) *developing or operating and maintaining or developing, operating and maintaining any infrastructure facility as defined in the Explanation to clause (i) of sub-section (4) of section 80-IA; or*
 - (ii) *dairy or poultry industry;*
- (24) any income chargeable under the heads “Income from house property” and “Income from other sources” of—
- (a) a registered union within the meaning of the Trade Unions Act, 1926 (16 of 1926), formed primarily for the purpose of regulating the relations between workmen and employers or between workmen and workmen;
 - (b) an association of registered unions referred to in sub-clause (a)

Case Law:

- (i) *Ancillary and incidental objects are not barred* - Section 10(24) does not lay down that the association must be formed *wholly and exclusively* for the purposes enumerated in that provision. An association registered under the Trade Unions Act, having other ancillary and incidental objects apart from the primary object of regulation between its members and their employees, is also entitled to exemption - *CIT v. Calcutta Hydraulic Press Association* 121 ITR 414 .
- (25) (i) interest on securities which are held by, or are the property of, any provident fund to which the Provident Funds Act, 1925 (19 of 1925), applies, and any capital gains of the fund arising from the sale, exchange or transfer of such securities;
- (ii) any income received by the trustees on behalf of a recognised provident fund;
- (iii) any income received by the trustees on behalf of an approved superannuation fund;
- (iv) any income received by the trustees on behalf of an approved gratuity fund;

- (v) any income received—
- (a) by the Board of Trustees constituted under the Coal Mines Provident Funds and Miscellaneous Provisions Act, 1948 (46 of 1948), on behalf of the Deposit-linked Insurance Fund established under section 3G of that Act; or
- (b) by the Board of Trustees constituted under the Employees' Provident Funds and Miscellaneous Provisions Act, 1952 (19 of 1952), on behalf of the Deposit-linked Insurance Fund established under section 6C of that Act

(25A) any income of the Employees' State Insurance Fund set up under the provisions of the Employees' State Insurance Act, 1948 (34 of 1948)

(26) in the case of a member of a Scheduled Tribe as defined in clause (25) of article 366 of the Constitution, residing in any area specified in Part I or Part II of the Table appended to paragraph 20 of the Sixth Schedule to the Constitution or in the [States of Arunachal Pradesh, Manipur, Mizoram, Nagaland and Tripura] or in the areas covered by notification No. TAD/R/35/50/109, dated the 23rd February, 1951, issued by the Governor of Assam under the proviso to sub-paragraph (3) of the said paragraph 20 [as it stood immediately before the commencement of the North-Eastern Areas (Reorganisation) Act, 1971 (81 of 1971)] [or in the Ladakh region of the State of Jammu and Kashmir], any income which accrues or arises to him,—

- (a) from any source in the areas or States aforesaid], or
- (b) by way of dividend or interest on securities;

Case Law:

- (i) *Provision is constitutionally valid* - Section 10(26)(a) is constitutionally valid. The classification therein for the purpose of exemption from tax between income from a specified area and income from outside that specified area is not discriminatory and does not offend article 14 of the Constitution - *ITO v. N. Takin Roy Rymbai* 103 ITR 82.

(26A) any income accruing or arising to any person from any source in the district of Ladakh or outside India in any previous year relevant to any assessment year commencing before the 1st day of April, [1989], where such person is resident in the said district in that previous year :

Provided that this clause shall not apply in the case of any such person unless he was resident in that district in the previous year relevant to the assessment year commencing on the 1st day of April, 1962.

[Explanation 1].—For the purposes of this clause, a person shall be deemed to be resident in the district of Ladakh if he fulfils the requirements of sub-section (1) or sub-section (2) or sub-section (3) or sub-section (4) of section 6, as the case may be, subject to the modifications that—

- (i) references in those sub-sections to India shall be construed as references to the said district; and
- (ii) in clause (i) of sub-section (3), reference to Indian company shall be construed as reference to a company formed and registered under any law for the time being in force in the State of Jammu and Kashmir and having its registered office in that district in that year.

[Explanation 2.—In this clause, references to the district of Ladakh shall be construed as references to the areas comprised in the said district on the 30th day of June, 1979;]

(26AAA) in case of an individual, being a Sikkimese, any income which accrues or arises to him

- (a) from any source in the State of Sikkim; or
- (b) by way of dividend or interest on securities:

Provided that nothing contained in this clause shall apply to a Sikkimese woman who, on or after the 1st day of April, 2008, marries an individual who is not a Sikkimese.



Explanation. For the purposes of this clause, Sikkimese shall mean

- (i) an individual, whose name is recorded in the register maintained under the Sikkim Subjects Regulation, 1961 read with the Sikkim Subject Rules, 1961 (hereinafter referred to as the Register of Sikkim Subjects), immediately before the 26th day of April, 1975; or
- (ii) an individual, whose name is included in the Register of Sikkim Subjects by virtue of the Government of India Order No. 26030/36/90-I.C.I., dated the 7th August, 1990 and Order of even number dated the 8th April, 1991; or
- (iii) any other individual, whose name does not appear in the Register of Sikkim Subjects, but it is established beyond doubt that the name of such individuals father or husband or paternal grand-father or brother from the same father has been recorded in that register;]

(26AAB) *any income of an agricultural produce market committee or board constituted under any law for the time being in force for the purpose of regulating the marketing of agricultural produce.*

(26B) any income of a corporation established by a Central, State or Provincial Act or of any other body, institution or association (being a body, institution or association wholly financed by Government) where such corporation or other body or institution or association has been established or formed for promoting the interests of the [members of the Scheduled Castes or the Scheduled Tribes or backward classes or of any two or all of them].

[Explanation.—For the purposes of this clause,—

- (a) Scheduled Castes” and Scheduled Tribes” shall have the meanings respectively assigned to them in clauses (24) and (25) of article 366 of the Constitution;
- (b) “backward classes” means such classes of citizens, other than the Scheduled Castes and the Scheduled Tribes, as may be notified—
 - (i) by the Central Government; or
 - (ii) by any State Government, as the case may be, from time to time;

(26BB) any income of a corporation established by the Central Government or any State Government for promoting the interests of the members of a minority community.

Explanation.—For the purposes of this clause, “minority community” means a community notified as such by the Central Government in the Official Gazette in this behalf;

(26BBB) any income of a corporation established by a Central, State or Provincial Act for the welfare and economic upliftment of ex-servicemen being the citizens of India.

Explanation.—For the purposes of this clause, “ex-serviceman” means a person who has served in any rank, whether as combatant or non-combatant, in the armed forces of the Union or armed forces of the Indian States before the commencement of the Constitution (but excluding the Assam Rifles, Defence Security Corps, General Reserve Engineering Force, Lok Sahayak Sena, Jammu and Kashmir Militia and Territorial Army) for a continuous period of not less than six months after attestation and has been released, otherwise than by way of dismissal or discharge on account of misconduct or inefficiency, and in the case of a deceased or incapacitated ex-serviceman includes his wife, children, father, mother, minor brother, widowed daughter and widowed sister, wholly dependant upon such ex-serviceman immediately before his death or incapacitation;

(27) any income of a co-operative society formed for promoting the interests of the members of either the Scheduled Castes or Scheduled Tribes or both referred to in clause (26B) :

Provided that the membership of the co-operative society consists of only other co-operative societies formed for similar purposes and the finances of the society are provided by the Government and such other societies;

(29A) any income accruing or arising to—

- (a) the Coffee Board constituted under section 4 of the Coffee Act, 1942 (7 of 1942) in any previous year relevant to any assessment year commencing on or after the 1st day of April, 1962 or the previous year in which such Board was constituted, whichever is later;

- (b) the Rubber Board constituted under sub-section (1) of section 4 of the Rubber Board Act, 1947 (24 of 1947) in any previous year relevant to any assessment year commencing on or after the 1st day of April, 1962 or the previous year in which such Board was constituted, whichever is later;
- (c) the Tea Board established under section 4 of the Tea Act, 1953 (29 of 1953) in any previous year relevant to any assessment year commencing on or after the 1st day of April, 1962 or the previous year in which such Board was constituted, whichever is later;
- (d) the Tobacco Board constituted under the Tobacco Board Act, 1975 (4 of 1975) in any previous year relevant to any assessment year commencing on or after the 1st day of April, 1975 or the previous year in which such Board was constituted, whichever is later;
- (e) the Marine Products Export Development Authority established under section 4 of the Marine Products Export Development Authority Act, 1972 (13 of 1972) in any previous year relevant to any assessment year commencing on or after the 1st day of April, 1972 or the previous year in which such Authority was constituted, whichever is later;
- (f) the Agricultural and Processed Food Products Export Development Authority established under section 4 of the Agricultural and Processed Food Products Export Development Act, 1985 (2 of 1986) in any previous year relevant to any assessment year commencing on or after the 1st day of April, 1985 or the previous year in which such Authority was constituted, whichever is later;
- (g) the Spices Board constituted under sub-section (1) of section 3 of the Spices Board Act, 1986 (10 of 1986) in any previous year relevant to any assessment year commencing on or after the 1st day of April, 1986 or the previous year in which such Board was constituted, whichever is later;

Case Law:

- (i) *Retrospective effect of introduction provisions of section 10(29A)(d)* - In view of the provisions of section 10(29A)(d) introduced by the Finance Act, 1999, the assessee-Tobacco Board's income would become exempt from income-tax for any assessment year with effect from 1-4-1975 or the previous year in which the Board was constituted and the assessments already made would stand set aside by virtue of section 10(29A)(d) with retrospective effect, and the assessee will also be entitled to refund consequent to the retrospective amendment passed by Parliament - *Tobacco Board v. CIT* 243 ITR 4 .
- (30) in the case of an assessee who carries on the business of growing and manufacturing tea in India, the amount of any subsidy received from or through the Tea Board under any such scheme for replantation or replacement of tea bushes [or for rejuvenation or consolidation of areas used for cultivation of tea] as the Central Government may, by notification in the Official Gazette, specify:

Provided that the assessee furnishes to the [Assessing] Officer, along with his return of income for the assessment year concerned or within such further time as the [Assessing] Officer may allow, a certificate from the Tea Board as to the amount of such subsidy paid to the assessee during the previous year.

Explanation.—In this clause, “Tea Board” means the Tea Board established under section 4 of the Tea Act, 1953 (29 of 1953)

Case Law:

- (i) *Scope of deduction* - Since expression ‘or for rejuvenation or consolidation of areas used for cultivation of tea’ was inserted in section 10(30) by Finance Act, 1984 with effect from 1-4-1985, benefit of deduction in respect of rejuvenation subsidy granted by Tea Board to assessee would be available only from assessment year 1985-86 and not for assessment year 1984-85 - *Kil Kotagiri Tea & Coffee Estate Co. Ltd. v. CIT* 108 Taxman 125.
- (31) in the case of an assessee who carries on the business of growing and manufacturing rubber, coffee, cardamom or such other commodity in India, as the Central Government may, by notification in the Official Gazette, specify in this behalf, the amount of any subsidy received from or through the concerned Board under any such scheme for replantation or replacement of rubber plants, coffee plants, cardamom plants or plants for the



growing of such other commodity or for rejuvenation or consolidation of areas used for cultivation of rubber, coffee, cardamom or such other commodity as the Central Government may, by notification in the Official Gazette, specify:

Provided that the assessee furnishes to the Assessing Officer, along with his return of income for the assessment year concerned or within such further time as the Assessing Officer may allow, a certificate from the concerned Board, as to the amount of such subsidy paid to the assessee during the previous year.

Explanation.—In this clause, “concerned Board” means,—

- (i) in relation to rubber, the Rubber Board constituted under section 4 of the Rubber Act, 1947 (24 of 1947),
 - (ii) in relation to coffee, the Coffee Board constituted under section 4 of the Coffee Act, 1942 (7 of 1942),
 - (iii) in relation to cardamom, the Spices Board constituted under section 3 of the Spices Board Act, 1986 (10 of 1986),
 - (iv) in relation to any other commodity specified under this clause, any Board or other authority established under any law for the time being in force which the Central Government may, by notification in the Official Gazette, specify in this behalf;
- (32) in the case of an assessee referred to in sub-section (1A) of section 64, any income includible in his total income under that sub-section, to the extent such income does not exceed one thousand five hundred rupees in respect of each minor child whose income is so includible;
- (33) any income arising from the transfer of a capital asset, being a unit of the Unit Scheme, 1964 referred to in Schedule I to the Unit Trust of India (Transfer of Undertaking and Repeal) Act, 2002 (58 of 2002) and where the transfer of such asset takes place on or after the 1st day of April, 2002;
- (34) any income by way of dividends referred to in section 115-O.

Explanation.—For the removal of doubts, it is hereby declared that the dividend referred to in section 115-O shall not be included in the total income of the assessee, being a Developer or entrepreneur;

- (35) any income by way of,—
- (a) income received in respect of the units of a Mutual Fund specified under clause (23D); or
 - (b) income received in respect of units from the Administrator of the specified undertaking; or
 - (c) income received in respect of units from the specified company:

Provided that this clause shall not apply to any income arising from transfer of units of the Administrator of the specified undertaking or of the specified company or of a mutual fund, as the case may be.

Explanation.—For the purposes of this clause,—

- (a) “Administrator” means the Administrator as referred to in clause (a) of section 2 of the Unit Trust of India (Transfer of Undertaking and Repeal) Act, 2002 (58 of 2002)
 - (b) “specified company” means a company as referred to in clause (h) of section 2 of the Unit Trust of India (Transfer of Undertaking and Repeal) Act, 2002 (58 of 2002)
- (36) any income arising from the transfer of a long-term capital asset, being an eligible equity share in a company purchased on or after the 1st day of March, 2003 and before the 1st day of March, 2004 and held for a period of twelve months or more.

Explanation.—For the purposes of this clause, “eligible equity share” means,—

- (i) any equity share in a company being a constituent of BSE-500 Index of the Stock Exchange, Mumbai as on the 1st day of March, 2003 and the transactions of purchase and sale of such equity share are entered into on a recognised stock exchange in India;
- (ii) any equity share in a company allotted through a public issue on or after the 1st day of March, 2003 and listed in a recognised stock exchange in India before the 1st day of March, 2004 and the transaction of sale of such share is entered into on a recognised stock exchange in India;

- (37) in the case of an assessee, being an individual or a Hindu undivided family, any income chargeable under the head “Capital gains” arising from the transfer of agricultural land, where—
- (i) such land is situate in any area referred to in item (a) or item (b) of sub-clause (iii) of clause (14) of section 2;
 - (ii) such land, during the period of two years immediately preceding the date of transfer, was being used for agricultural purposes by such Hindu undivided family or individual or a parent of his;
 - (iii) such transfer is by way of compulsory acquisition under any law, or a transfer the consideration for which is determined or approved by the Central Government or the Reserve Bank of India;
 - (iv) such income has arisen from the compensation or consideration for such transfer received by such assessee on or after the 1st day of April, 2004.

Explanation.—For the purposes of this clause, the expression “compensation or consideration” includes the compensation or consideration enhanced or further enhanced by any court, Tribunal or other authority;

- (38) any income arising from the transfer of a long-term capital asset, being an equity share in a company or a unit of an equity oriented fund where—
- (a) the transaction of sale of such equity share or unit is entered into on or after the date on which Chapter VII of the Finance (No. 2) Act, 2004 comes into force; and of power where such transfer is effected on or before the 31st day of March, 2006, to the Indian company notified under sub-clause (a) of clause (v) of sub-section (4) of section 80-IA;
- (38) any income arising from the transfer of a long-term capital asset, being an equity share in a company or a unit of an equity oriented fund where
- (a) the transaction of sale of such equity share or unit is entered into on or after the date on which Chapter VII of the Finance (No. 2) Act, 2004 comes into force; and
 - (b) such transaction is chargeable to securities transaction tax under that Chapter :

[Provided that the income by way of long-term capital gain of a company shall be taken into account in computing the book profit and income-tax payable under [section 115JB](#).]

Explanation.For the purposes of this clause, equity oriented fund means a fund

- (i) where the investible funds are invested by way of equity shares in domestic companies to the extent of more than [sixty-five] per cent of the total proceeds of such fund; and
- (ii) which has been set up under a scheme of a Mutual Fund specified under clause (23D) :

Provided that the percentage of equity shareholding of the fund shall be computed with reference to the annual average of the monthly averages of the opening and closing figures;]

- (39) any specified income, arising from any international sporting event held in India, to the person or persons notified by the Central Government in the Official Gazette, if such international sporting event
- (a) is approved by the international body regulating the international sport relating to such event;
 - (b) has participation by more than two countries;
 - (c) is notified by the Central Government in the Official Gazette for the purposes of this clause.

Explanation. For the purposes of this clause, the specified income means the income, of the nature and to the extent, arising from the international sporting event, which the Central Government may notify in this behalf;

- (40) any income of any subsidiary company by way of grant or otherwise received from an Indian company, being its holding company engaged in the business of generation or transmission or distribution of power if receipt of such income is for settlement of dues in connection with reconstruction or revival of an existing business of power generation:

Provided that the provisions of this clause shall apply if reconstruction or revival of any existing business of power generation is by way of transfer of such business to the Indian company notified under sub-clause (a) of clause (v) of sub-section (4) of [section 80-IA](#);



(41) any income arising from transfer of a capital asset, being an asset of an undertaking engaged in the business of generation or transmission or distribution of power where such transfer is effected on or before the 31st day of March, 2006, to the Indian company notified under sub-clause (a) of clause (v) of sub-section (4) of section 80-IA;

(42) any specified income arising to a body or authority which—

- (a) has been established or constituted or appointed under a treaty or an agreement entered into by the Central Government with two or more countries or a convention signed by the Central Government;
- (b) is established or constituted or appointed not for the purposes of profit;
- (c) is notified by the Central Government in the Official Gazette for the purposes of this clause.

Explanation.—For the purposes of this clause, “specified income” means the income, of the nature and to the extent, arising to the body or authority referred to in this clause, which the Central Government may notify in this behalf.

(43) any amount received by an individual as a loan, either in lump sum or in instalment, in a transaction of reverse mortgage referred to in clause (xvi) of section 47;

(44) *any income received by any person for, or on behalf of, the New Pension System Trust established on the 27th day of February, 2008 under the provisions of the Indian Trusts Act, 1882 (2 of 1882).*

Tax exemption in case of newly established industrial undertakings in free trade zones [Sec. 10A (Rule - 16D)]

Profits or gains of exports of newly established Industrial undertakings set up in Free Trade Zones, Electronic Hardware Technology Park or software Technology Park special economic zone are fully exempt for ten consecutive Assessment Years beginning with the AY relevant to the Previous Year in which the industrial undertakings begin to manufacture or produce articles or things or computer software specified by the assessee. No deduction under this section is available for the Assessment Year beginning on 1.4.2010 and subsequent years. W.e.f. AY 2003-04, Sec. 10A(1A) has been inserted to provide exemption in computing income of an undertaking which begins to manufacture or produce articles or things or computer software during the Previous Year relevant to AY commencing on or after 1.4.2003 in any special economic zone, and which shall be 100% of profits and gains derived from export of such articles or things or computer software for a period of 5 consecutive years being with the AY relevant to the Previous Year in which the undertaking begins to manufacture or produce such article or thing or computer software as the case may be and thereafter 50% of such profits and gains for further two Assessment Years. Exemptions will also be available to successor company w.e.f. AY 2003-04 in case of business reorganisation – S.10A(9A) for AY 2003-04 exemption is restricted to 90% of the profit.

Sec. 10A (IA): The Finance Act, 2005 has inserted a proviso to provide that no deduction shall be allowed under this section to an assessee who does not furnish a return of his income on or before the due date specified under sub-section (1) of section 139. Return of income of SEZ undertakings to be filed on or before due date for claiming benefit under section 10A, w.e.f. from A.Y. 2006-07: Sub-section (1A) OF SECTION 10A provides that an undertaking which begins to manufacture or produce articles or things or computer software during the previous year relevant any assessment year commencing on or after 1st April, 2003 in any special economic zone (SEZ), is eligible for a deduction, 100% of the profits and gains derived from export of such articles or things or computer software for the first five consecutive years and 50% of such profits and gains for the next two consecutive years followed by a deduction to the extent of 50% of profits credited to a reserve account to be utilized for the purpose of the business for the next three consecutive years. A proviso has been inserted to the said sub-section so as to provide that no deduction under section 10A shall be allowed to an assessee who does not furnish a return of his Income on or before the due date specified u/s 139(1)

Tax in respect of 100% exports oriented undertaking concession [Sec. 10B]

Profit or gains of export derived from 100% export oriented unit (EOU) is exempt from tax for 10 consecutive years beginning with the initial Assessment Year in which the undertaking begins to manufacture or produce articles or things or computer software. This tax concession is available to all tax payers including companies in lieu of all other tax concessions.

Conditions for tax exemptions are that:

- (i) it is a manufacturing undertaking;
- (ii) it is not formed by splitting up or the reconstruction of a business already in advance.
- (iii) it should not use old machinery valued more than 20% of the value of total plant and machinery.

- (iv) no deduction under section 80HH, 80HHA, 80-I and 80-IA shall be allowed in relation to the profits and gains of the undertaking. Exemption is also available to Successor company in case of reorganisation 10B (9A) w.e.f. AY 2003-04. For the Assessment Year 2003-04, exemption is restricted to 90% of the profit.

Case Law :

- (i) *Scope of exemptions* - Since section 10B provides 100 per cent exemption for export income and not for other income, assessee cannot adjust unabsorbed depreciation against other income so as to take exemption from payment of tax even for other income - *CIT v. Himatasingike Seide Ltd.* 156 Taxman 151.

Extension of sunset clause for units in free trade zone under section 10A and for export oriented undertakings under section 10B by one year i.e., the deduction will be available up to assessment year 2011-12 [Section 10A and 10B]

Under the existing provisions, the deductions under section 10A and section 10B of the Income Tax Act are available only up to the assessment year 2010-11. The Act has amended sections 10A and 10B to extend the tax benefit under both these sections by one year i.e., the deduction will be available up to assessment year 2011-12 or for a period of 10 years whichever expires earlier.

Clarification regarding computation of exempted profits in the case of units in Special Economic Zones (SEZs) — Computed with reference to the total turnover of the “undertaking” instead of “the business carried on by the assessee” [Section 10AA][W.e.f. A.Y. 2010-11]

Under section 10AA(7) of the Income-tax Act, the exempted profit of a SEZ unit is the profit derived from the export of articles or things or services and same is required to be calculated as under :

The exempted profit of the SEZ unit is equal to

$$\text{Profits of the business of the unit} \times \frac{\text{Export turnover of the unit}}{\text{Total turnover of the business carried on by the assessee}}$$

(Now changed to total turnover of the undertaking)

This method of computation of the profits of business with reference to the total turnover of the assessee is perceived to be discriminatory in so far as those assesseees are concerned who were having multiple units in both the SEZ and the domestic tariff area (DTA) vis-a-vis those assesseees who were having units in only the SEZ. With a view to remove the anomaly, the Act has amended the provisions of section 10AA(7) of the Income Tax Act so as to provide that the deduction under section 10AA shall be computed with reference to the total turnover of the undertaking.

Meaning of computer programmes in certain cases [Sec.10BB]

The profits and gains derived by an undertaking from the production of computer programmes under section 10B, as it stood prior to its substitution by section 7 of the Finance Act, 2000 (10 of 2000), shall be construed as if for the words “computer programmes”, the words “computer programmes or processing or management of electronic data” had been substituted in that section.]

Special provision in respect of certain industrial undertakings in North- Eastern Region [10C]

- (1) Subject to the provisions of this section, any profits and gains derived by an assessee from an industrial undertaking, which has begun or begins to manufacture or produce any article or thing on or after the 1st day of April, 1998 in any Integrated Infrastructure Development Centre or Industrial Growth Centre located in the North-Eastern Region (hereafter in this section referred to as the industrial undertaking) shall not be included in the total income of the assessee.
- (2) This section applies to any industrial undertaking which fulfils all the following conditions, namely :—
 - (i) it is not formed by the splitting up, or the reconstruction of, a business already in existence :
Provided that this condition shall not apply in respect of any industrial undertaking which is formed as a result of the re-establishment, reconstruction or revival by the assessee of the business of any such industrial undertaking as is referred to in section 33B, in the circumstances and within the period specified in that section ;
 - (ii) it is not formed by the transfer to a new business of machinery or plant previously used for any purpose.
- (3) The profits and gains referred to in sub-section (1) shall not be included in the total income of the assessee in respect of ten consecutive assessment years beginning with the assessment year relevant to the previous year in which the industrial undertaking begins to manufacture or produce articles or things.



- (4) Notwithstanding anything contained in any other provision of this Act, in computing the total income of the assessee of any previous year relevant to any subsequent assessment year,—
 - (i) section 32, section 35 and clause (ix) of sub-section (1) of section 36 shall apply as if deduction referred to therein and relating to or allowable for any of the relevant assessment years, in relation to any building, machinery, plant or furniture used for the purposes of the business of the industrial undertaking in the previous year relevant to such assessment year or any expenditure incurred for the purposes of such business in such previous year had been given full effect to for that assessment year itself and, accordingly, sub-section (2) of section 32, sub-section (4) of section 35 or the second proviso to clause (ix) of sub-section (1) of section 36, as the case may be, shall not apply in relation to any such deduction;
 - (ii) no loss referred to in sub-section (1) of section 72 or sub-section (1) or sub-section (3) of section 74, in so far as such loss relates to the business of the industrial undertaking, shall be carried forward or set off where such loss relates to any of the relevant assessment years;
 - (iii) no deduction shall be allowed under section 80HH or section 80HHA or section 80-I or section 80-IA or section 80-IB or section 80JJA in relation to the profits and gains of the industrial undertakings; and
 - (iv) in computing the depreciation allowance under section 32, the written down value of any asset used for the purposes of the business of the industrial undertaking shall be computed as if the assessee had claimed and been actually allowed the deduction in respect of depreciation for each of the relevant assessment years.
- (5) The provisions of sub-section (8) and sub-section (10) of section 80-IA shall, so far as may be, apply in relation to the industrial undertaking referred to in this section as they apply for the purposes of the industrial undertaking referred to in section 80-IA or section 80-IB, as the case may be.
- (6) Notwithstanding anything contained in the foregoing provisions of this section, where the assessee before the due date for furnishing the return of his income under sub-section (1) of section 139, furnishes to the Assessing Officer a declaration in writing that the provisions of this section may not be made applicable to him, the provisions of this section shall not apply to him in any of the relevant assessment years :

Income of trusts or institutions from contributions [Sec. 12]

- (1) Any voluntary contributions received by a trust created wholly for charitable or religious purposes or by an institution established wholly for such purposes (not being contributions made with a specific direction that they shall form part of the corpus of the trust or institution) shall for the purposes of section 11 be deemed to be income derived from property held under trust wholly for charitable or religious purposes and the provisions of that section and section 13 shall apply accordingly.
- (2) The value of any services, being medical or educational services, made available by any charitable or religious trust running a hospital or medical institution or an educational institution, to any person referred to in clause (a) or clause (b) or clause (c) or clause (cc) or clause (d) of sub-section (3) of section 13, shall be deemed to be income of such trust or institution derived from property held under trust wholly for charitable or religious purposes during the previous year in which such services are so provided and shall be chargeable to income-tax notwithstanding the provisions of sub-section (1) of section 11.
- (3) Notwithstanding anything contained in section 11, any amount of donation received by the trust or institution in terms of clause (d) of sub-section (2) of section 80G in respect of which accounts of income and expenditure have not been rendered to the authority prescribed under clause (v) of sub-section (5C) of that section, in the manner specified in that clause, or which has been utilised for purposes other than providing relief to the victims of earthquake in Gujarat or which remains unutilised in terms of sub-section (5C) of section 80G and not transferred to the Prime Minister's National Relief Fund on or before the 31st day of March, 2004 shall be deemed to be the income of the previous year and shall accordingly be charged to tax.

Case Law:

- (i) Specific directive to apply for charitable/religious purposes is necessary - The most relevant condition is that the contributions are applicable solely to charitable or religious purposes. It is implied that there has to be a specific directive for applying the donations solely for charitable or religious purposes - *R.B. Shreeram Religious & Charitable Trust v. CIT* 172 ITR 373.

ILLUSTRATIONS ON INCOME EXEMPT FROM TAX

Illustration 1. B Ltd. owns a new industrial undertaking, located in industrially backward State. It has been approved 100% EOU by the Board, constituted by the Central Government. It is engaged in the export of computer software and started functioning from the previous year 2007-2008.

During the first three years it earned a profits and claimed deduction under Sec. 10B. During the fourth year it suffered a loss of ₹ 10 lakh.

It furnishes the following particulars for the previous year 2011-2012.

	₹ (in lakh)
(i) Business profit	40
(ii) Export sales – FOB	100
(iii) Domestic sales	50
(iv) Receipt of convertible foreign exchange in India :	
(a) Receipt up to 30 September 2012	70
However, foreign exchange of ₹ 10 lakh is on account of sale to a foreign customer in India and ₹ 5 lakh is on account of reimbursement of freight, insurance, relating to export export and expenses incurred in Malaya in foreign exchange in providing technical services.	
(b) Receipt in November 2012 but approved by the competent authority	10
(c) Receipt in January 2013 but competent authority has not granted its approval	10
(v) Converted foreign exchange kept in Malaya in State Bank of India in a separate account with the approval of RBI.	10

Compute its total income in the following cases :

- (a) it claims deduction under Sec. 10B;
- (b) it revises its option under Sec. 10B(8) and wants not to claim deduction under Sec. 10B. it proposes to claim deduction under Sec. 80 IB.

Solution: (i) Claiming deduction under Sec. 10B

	₹ (in lakh)
Business profits	40
Less : Deduction for export profits : $40 \times \frac{75}{150}$	20
	20
Less : Carried forward business loss [Sec. 72 (2)]	<u>10</u>
Total income	<u>10</u>

Working Note :

1. Export turnover :	
Convertible foreign exchange received up to 30 September 2012	
Less : (i) Convertible foreign exchange received from a foreign customer for sale in India	70
(ii) Reimbursement of foreign insurance relating to export and expenses incurred in foreign exchange outside India in providing technical services.	(-) 10
	(-) 5
Add: (i) Convertible foreign exchange received after prescribed time limit but approved by the competent authority	(+) 10
(ii) Convertible foreign exchange kept outside India with the permission of Reserve Bank of India	<u>(+) 10</u>
	<u>75</u>



2. Total turnover :	100
(i) Export sales	<u>50</u>
(ii) Domestic Sales	<u>150</u>
(ii) Claiming deduction under Sec. 80-IB	
Business profits	40
Less : Carried forward business loss	<u>(-) 10</u>
Gross total income	30
Less : Deduction under Sec. 80-IB 100% of profits derived from undertaking and included in GTI	<u>30</u>
Total Income	<u>Nil</u>

Illustration 2. H Bros., an HUF, started an undertaking in “Special Economic Zone” during the previous year 2007-2008. From the following particulars relating to the previous year 2011-2012, compute the total income for the assessment year 2012-2013 :

	₹ (in lakh)
(i) Total turnover	30
(ii) Export sales	25
(iii) Business profits	15
(iv) Receipt of convertible foreign exchange in India up to 30 September 2012	
(v) Convertible foreign exchange kept outside India with the permission of RBI for importing a new machinery	16
(vi) Receipt of convertible foreign exchange in December 2012	4
(vii) Convertible foreign exchange received for reimbursement for freight, insurance attributable to export	2

Solution : Computation of total income

	₹ (in lakh)
Business profits	15
Less : Deduction for export profits : $15 \times \frac{20}{30}$ [Sec. 10A]	<u>10</u>
Total income	<u>5</u>

Note :

1. Convertible foreign exchange received in December 2011 has not been included in Export turnover, because it is received after the prescribed time limit without approval of the competent authority.
2. Convertible foreign exchange kept outside India with the permission of RBI is included in Export turnover.
3. Reimbursement of freight and insurance in convertible foreign exchange is not included in Export turnover.

Illustration 3. Z has set up a new undertaking at Durgapur during the year 2011-2012 :

Compute taxable profits from the information given below:

Particulars	₹ (in lakh)
(i) Total turnover	50
(ii) Export sales	48
(iii) Export turnover	40
(iv) Business profit	30

- (v) 20 workers were employed during the year, and 18% plant and machinery are second-hand.
- (vi) Imported raw material was not used.

Will your answer be different in the following cases :

- (i) Number of workers employed during the year is 19.
- (ii) Number of permanent workers are 15 and number of temporary workers are 5.
- (iii) Export sales are ₹ 44.99 lakh.
- (iv) Percentage of old plant and machinery is 20.5%
- (v) 5% raw material was imported from Japan due to domestic shortage.
- (vi) ₹ 5 lakh convertible foreign exchange was received but kept outside India to import new machinery without the approval of RBI.

Solution :	Computation of total income	A. Y : 2012-13
		₹ (in lakh)
Business profits		30
Less : Deduction for export profits [Sec. 10BA] : $30 \times \frac{40}{50}$		24
Total Income		<u>6</u>

Comments :

- (i) No deduction will be available as the number of workers is below 20
- (ii) Deduction will be allowed. Number of workers should 20 whether permanent or temporary, regular or casuals.
- (iii) No deduction will be allowed. Export sales are less than 90% of total turnover.
- (iv) No deduction will be allowed. Percentage of old plant and machinery is more than 20% of the total investment in new plant and machinery.
- (v) No deduction will be allowed as raw material has been imported.

Solution :	Computation of Total Income	A. Y : 2012-13
		₹ (in lakh)
Business profits		30
Less : Deduction for export profits [Sec. 10BA] : $30 \times \frac{35}{50}$		21
Total Income		<u>9</u>

Illustration 4. The books of account maintained by a National Political Party registered under the Representation of the People Act, 1951 for the year ended on 31-3-2012 disclose the following receipts :

(a) Rent of property let out to a departmental store at Chennai.	10,00,000
(b) Interest on deposits other than banks.	2,00,000
(c) Contribution from 100 persons (who have secreted their names) of ₹ 33,000 each	33,00,000
(d) Contribution @ ₹ 22 each from 1,00,000 members in cash	22,00,000
(e) Net profit of cafeteria run in the premises at Delhi	3,00,000

Compute the total income of the political party for the assessment year 2012-2013, with reason for inclusion or otherwise.



Solution : Computation of income of National Political Party: AY 2012-2013

Particulars	₹
(a) Rent from property: Exempt under Sec. 13A	—
(b) Income from business—Profits of cafeteria	3,00,000
(c) Income other sources:	—
(i) Interest on deposit other than banks: Exempt under Sec. 13A	—
(ii) Contributions from 100 persons exceeding ₹ 22,000 each—See Note below,	33,00,000
(iii) Contributions from 1,00,000 members: Exempt Sec. 13A.	—
Total Income	36,00,000

Note : Any income of a political party received by way of voluntary contributions is exempt, provided:

- (i) it keeps and maintains such books of account and other documents as would enable the Assessing Officer to properly deduce its income therefrom;
- (ii) it keeps and maintains a record, name and address of the person who has contributed in excess of ₹ 20,000; and
- (iii) its accounts are audited by an accountant defined in Explanation below Sec. 288(2).

Thus, in order to claim exemption in respect of voluntary contributions exceeding ₹ 20,000, a political party is required to keep and maintain a record, and names, address of persons who have made such contributions. The legislative intention is to ensure that there is transparency in the process of collection of funds [Common Cause v. Vol. 222 ITR 260 (SC)]. Hence, no exemption can be allowed in respect of contributions exceeding ₹ 20,000 from persons who have secreted their names.

Illustration 5. A company is engaged in the development and sale of computer software applications. It has started a new undertaking for which approval as a 100% export-oriented undertaking has been obtained from the CBDT. It furnishes the following data and requests you to compute the deduction allowable to it under Sec. 10B in respect of assessment year 2012-2013.

Particulars	₹ (in lakh)
Total profit of the company for the previous year	50
Total turnover, i.e. Export sales and Domestic sales for the previous year	500
Consideration received in respect of export of software received in convertible foreign exchange within 6 months of the end of the previous year	250
Sale proceeds credited to a separate account in a bank outside India with the approval of RBI	50
Telecom and insurance charges attributable to export of software	10
Staff costs and travel expenses incurred in foreign exchange to provide technical assistance outside India to a client	40

Solution : Computation of income of a 100% export-oriented undertaking: AY 2012-2013

Particulars	₹ (in lakh)
Total profit	50
Less: Deduction under Sec. 10B: $\frac{\text{Export turnover} \times \text{Total profits}}{\text{Total turnover}} = 50 \times \frac{250}{500} =$	25
Taxable profits	25

Note :

Export turnover	(₹ in lakh)
(i) Sale proceeds of software received in convertible foreign exchange within the prescribed period	250
(ii) Sale proceed in convertible foreign exchange kept outside India with the approval of RBI	50
	300
Less : (i) Telecom and insurance attributable to export turnover	(-) 10
(ii) Expenses incurred in foreign exchange outside India to provide technical assistance to a client there	(-) 40
Export turnover	<u>250</u>

Illustration 6. XY & Co., a partnership concern had established an undertaking for manufacturing computer software in Free Trade Zone. It furnishes the following particulars of its second year operations, ending on 31-03-2012:

Particulars	₹ (in lakh)
Total sales of business	100.00
Export sales	80.00
Profit of the business	10.00

Out of the total sales, realisation of sale of ₹ 5 lakh is difficult because of the deficiency of the buyer. Realisation of rest of the sales is received in time.

The plant and machinery used in the business had been depreciated @ 15% on SLM basis of depreciation and depreciation of ₹ 3 lakh was charged to the Profit and Loss Account.

Compute the taxable income of XY & Co for the assessment year 2012-2013.

Solution:

Computation of Taxable Income for the A.Y. 2012-13

Particulars	₹ (in lakh)
Profit of business	10,00,000
Add : Depreciation charged on SLM basis	30,000
	<u>1,30,000</u>
Less : Depreciation on WDV basis @ 15% of 17,00,000 – [See Note below]	2,55,000
	<u>10,45,000</u>
Less : Deduction under Sec. 10A : $10,45,000 \times 75 \div 100$	7,83,750
Taxable income	<u>2,61,250</u>

Note :

₹

1. Computation of Depreciation :

Total purchase price of machine : $3,00,000 \times 15 \div 100$	20,00,000
Less : Depreciation in the first year @ 15%	3,00,000
WDV at the end of first year	17,00,000
Less: Depreciation for second year @ 15%	2,55,000
WDV at the end of second year	<u>14,45,000</u>

2. Export Turnover:

Export Sales	80,00,000
Less: Remittance not received due to insolvency of buyer	5,00,000
	<u>75,00,000</u>



STUDY NOTE - 13

AGRICULTURAL INCOME AND AGGREGATION OF INCOMES

This Study Note includes

- Provisions under the Income Tax Act relating to Agricultural Income

13.1 AGRICULTURAL INCOME AND TAX LIABILITY

Article 270 of the Constitution of India empowers Government of India to collect tax on income other than agricultural income. Agricultural income has been placed in the State list and as such the Central Government cannot levy tax on agricultural income.

Sec. 2(1A) provides definition of the term. 'Agricultural income' means –

- any rent or revenue derived from land which is situated in India and is used for agricultural purposes.
- any income derived from such land by-
 - agriculture; or
 - the performance by a cultivator or receiver of rent-in-kind of any process ordinarily employed by a cultivator or receiver of rent-in-kind to render the produce raised or received by him fit to be taken to market; or
 - the sale by a cultivator or receiver of rent in kind of the produce raised or received by him, in respect of which no process has been raised or received by him, in respect of which no process has been performed other than a process of the nature described in para (ii) of the sub-clause:
- any income derived from any building owned and occupied by the receiver of rent or revenue of any such land provided the following conditions are satisfied-
 - the building should be on or in the immediate vicinity of land and is used for agricultural purposes;
 - the cultivator or receiver of rent-in-kind uses the building as a dwelling house or a store house; and
 - the land is assessed to land revenue or local rate or the land is situated within the jurisdiction of municipality/cantonment having a population of not less than 10,000 persons or within distance of not more than 8 k.m.

It may be pointed out that sec. 10(1) exempts from income-tax 'agricultural income' covered by the aforesaid definition.

However, in case of certain category of assessee e.g. individuals. HUFs having income more than maximum amount not liable for tax, 'agricultural income' is taken into consideration to determine tax on non-agricultural income.

Case Laws:

Essential Conditions :

Agriculture not involving any basic operation like tilling, sowing or dissemination of seeds and planting on land would not constitute agriculture merely because they have relation or connection with land. Term agriculture does

not include breeding and rearing of live stock, dairy farming, butter, cheese making, poultry, etc.- CIT v/s Raja Benoy Kumar Sahas Roy 32 ITR 466 (SC).

Agricultural Income :

Where the owner himself performs slaughter tapping and then sells the rubber, the income is agricultural income.- Jacob(K.C.) v Ag. ITO 110 ITR 402.

Lease rent received for leasing out land for grazing of cattle required for agricultural pursuits, is agricultural income.- CIT v Rai Shamsheerjang Bahadur 24 ITR 1.

Compensation received from an insurance company on account of damaged caused to the crop is an agricultural income.- CIT v B. Gupta Tea Pvt. Ltd. 74 ITR 337.

Seeds are clearly a product of agriculture and the income derived from the sale of seeds derived on account of cultivation by the assessee is an agricultural income.- CIT v Soundharya Nursury 241 ITR 530.

Miscellaneous income from plantation: Miscellaneous income from plantation should also be agricultural income except in respect of sale of trees of spontaneous growth. Thus, where a state undertaking owing a forest, had received income by sale of firewood, grazing permits and compounding fee for trespasses into the plantation, the same shall be treated as agricultural income.-CIT v Tamil Nadu Forest Plantation Corporation 248 ITR 331.

Non Agricultural Income :

Dividend received from company having only agricultural income is not agricultural income for a shareholder-CIT v/s Mrs. Bacha F. Guzdar 27 ITR 1 (SC).

Conversion of sugarcane into Gur- No Agriculture income - Seth Banarasi Dass Gupta v/s CIT. 106 ITR 804 .

Income from agricultural lands situated outside India is not agricultural income within the meaning of the Indian income-tax. Similarly if there is a figure of loss from agricultural lands, situated outside India, it has got to be deducted while computing the total income of the resident assessee in India - CIT v. Carew & Co. Ltd. 120 ITR 540.

Compensation for acquisition of land - Where land of assessee-tea company was requisitioned by State Government and same was given to refugees who carried on cultivation thereon and at time of requisition assessee too was carrying on agricultural operations on land, compensation received by assessee was to be treated as agricultural income - CIT v. All India Tea & Trading Co. Ltd. 85 Taxman 391/219 ITR 544.

Following are certain instances defining the scope of agricultural income.

Rent or revenue should be derived from land:

- Any loan obtained by a shareholder out of accumulated profits of the company having only agricultural income, which is liable to be treated as 'deemed dividend', is not agricultural income in the hands of recipient.
- Interest on arrears of cess or rent payable by a tenant to his landlord is no doubt revenue but it is not revenue derived from land and hence it is not agricultural income.
- Commission earned by a broker for selling agricultural produce of an agriculturist is not agricultural income.
- Any capital gain arising from the transfer of agricultural land is not treated as revenue derived from land and hence it is not agricultural income.

Income held as not derived from land:

- Mutation fees paid by tenant on succession to a holding by inheritance.
- Fees paid by tenants for renewal of leases and fees paid for recognising the distribution of holding on partition would not be income derived from land, since they are payments made for administrative services rendered by the landlord, akin to registration fees.



- Receipts from the supply of water tank in an agricultural land

Use of building or land for agricultural purpose:

- Any income arising from the use of land or building for any purpose (including letting for residential purpose or for the purpose of any business or profession) other than agriculture shall not be agricultural income.
- Any income attributable to farm house situated in urban areas will not be treated as agricultural income unless the land on which the farm house is situated is assessed to land revenue or any local rate. On the other hand, in case of farm house situated in rural areas, the income will be treated as agricultural income even where the land on which farm house is situated is not assessed to land revenue or any local rate.

Agriculture Income and Income-tax :

Agricultural income [Section 10(1)] –

- Section 10(1) provides that agricultural income is not to be included in the total income of the assessee. The reason for totally exempting agricultural income from the scope of central income tax is that under the Constitution, the Parliament has no power to levy a tax on agricultural income.
- Indirect way of taxing agricultural income - However, since 1973, a method has been found out to levy tax on agricultural income in an indirect way. This concept is known as partial integration of taxes. It is applicable to individuals, HUF, unregistered firms, AOP, BOI and artificial persons.

Two conditions which need to be satisfied for partial integration are:

1. The net agricultural income should exceed ₹5,000 for the year and
2. Non-agricultural income should exceed the maximum amount not chargeable to tax. (e. g. ₹ 2,40,000 for senior citizens, ₹ 1,90,000 for women assessee below 65 years of age, ₹ 1,60,000 for all other individuals and HUFs.)

It may be noted that aggregation provisions do not apply to company, firm assessed as such (FAS), co-operative society and local authority. The object of aggregating the net agricultural income with non-agricultural income is to tax the non-agricultural income at higher rates.

Tax calculation in such cases is as follows :

- Step 1:** Add non-agricultural income with net agricultural income. Compute tax on the aggregate amount.
- Step 2:** Add net agricultural income and the maximum exemption limit available to the assessee (e.g. ₹ 1,80,000 / ₹ 1,90,000 / ₹ 2,50,000, etc. as applicable). Compute tax on the aggregate amount.
- Step 3:** Deduct the amount of income tax calculated in step 2 from the income tax calculated in step 1 i.e. Step 1 – Step 2.
- Step 4:** Deduct any applicable rebate from the amount of tax obtained in step 3.
- Step 5:** Add surcharge, if applicable, to the amount obtained in step 4 above.
- Step 6:** The sum so arrived at shall be increased by education and higher secondary cess.

These steps are applicable whenever tax liability is to be worked out e.g. self-assessment tax, advance tax, tax on regular assessment)

ILLUSTRATIONS ON AGRICULTURAL INCOME AND TAX LIABILITY

Illustration 1. Mr X furnishes the return of income for the financial year 2011-2012. His total income (nonagricultural) is ₹ 12,10,000 and net agricultural income is ₹ 1,90,000. Compute the amount of tax payable by Mr X for the assessment year 2012-2013.

Solution : Computation of tax for the assessment year 2012-2013

- (a) Income tax on the aggregate of non-agricultural income and net agricultural income (i.e. ₹ 14,00,000) as if it is the total income.

On the first	1,80,000	Nil	Nil
On the next	3,20,000	10%	32,000
On the next	3,00,000	20%	60,000
On the balance	6,00,000	30%	1,80,000
	14,00,000		2,72,000

- (b) Income tax on net agricultural income plus the basic exemption limit i.e. ₹ 1,80,000 (i.e. ₹ 3,50,000) as if it is the total income.

On the first	1,80,000	Nil	Nil
On the next	1,70,000	10%	17,000
	3,50,000		17,000

Net income tax : (a) – (b) = ₹ 2,72,000 – 17,000 =	2,55,000
Add:	
(i) Education cess @ 2%	5,100
(ii) SHEC @ 1%	2,550
Tax payable	2,62,650

Illustration 2. Mr. Gangaprasad, resident in India, turns out 65 years of age on 31st December 2011. He furnishes the following particulars of his income for the previous year 2011-2012 :

Particulars	₹
(i) Rent from agriculture land, located in a village of Jharkhand district	2,50,000
(ii) Rent from building, located in the vicinity of agriculture land, which is assessed to land to revenue and the tenant, cultivating the agricultural land, occupies it for his dwelling and storing purposes	60,000
(iii) Income from business	3,00,000
(iv) Long-term capital gain	1,00,000

He maintains a motor car which is used 70% for business purpose, 10% for collecting rent from building and 20% for collecting rent from agriculture land. He has incurred an expenditure of ₹1,00,000 by way of petrol, repair and salary of the driver. He also claims depreciation on the written down value of the motor car on 1.4.2011. ₹ 2,00,000 @ 15%. He has paid ₹ 2000 as local tax to the village panchayat in respect of the building. He also paid ₹ 30,000 land revenue to the Government on account of agriculture land.

Determine his total income and tax liability in the following cases:

- Agriculture produce goes under marketing process to fetch better rates in the market,
- Agriculture produce goes under marketing process to make it saleable in the local market.



Solution :

Computation of Total Income for the Assessment Year 2012-2013

(i) Income from House Property: Gross annual value based on rent	60,000	
Less : Local tax to village panchayat: No deduction is allowed as— it is not a municipal tax	Nil	
Net Annual Value (NAV)	60,000	
Less: (i) Statutory deduction @ 30% of NAV	18,000	
Income from House Property		42,000
Income from house property to be treated as agriculture income provided the agriculture produce is not subjected to marketing produce to fetch better rates [Sec. 2(1A)(c)]		
(ii) Income from business		3,00,000
(iii) Long-term capital gain		1,00,000
(iv) Income from other sources :		
Rent from agriculture land	2,50,000	
Less: Permissible deduction (Sec. 57) :		
(a) Land revenue	(-) 30,000	
(b) Realisation expenses	(-) 20,000	
(c) Depreciation: Not admissible Sec. 57(ii) (see Note below)		
Income from agriculture [Sec. 2(1A)(a)]	2,00,000	
Total income , subject to increase by ₹ 42,000 when produce is subjected to marketing process to fetch better rates.		4,42,000

Computation of Tax Liability : AY. 2012-2013

Particulars	Senior citizen	
	Case I Produce subjected to marketing process for better rates ₹	Case II Produce subjected to marketing process to make it saleable ₹
Non-agriculture income	4,42,000	4,00,000
Agriculture income	2,00,000	2,42,000
Total Income	6,42,000	6,42,000
(a) Tax on non-agriculture income + agriculture income as if it is the total income:		
(i) Tax on long-term capital gain	20,000	20,000
(ii) Tax on balance of total income at slab rates	26,200	26,200
Gross Tax Liability (i) + (ii)	46,200	46,200
(b) Tax on agriculture income + basic exemption limit	20,000	24,200
(c) Tax payable: (a) – (b)	26,200	22,200
Add: Education cess @ 2%	524	440
SHEC @ 1%	262	220
Tax payable	29,986	22,660
Tax payable to be rounded off to the nearest multiple of ₹ 10 (Sec. 288B)	26,990	22,660

Note :

While computing income under “other sources” depreciation is allowed only in case where plant, machinery or furniture is let out on hire or building along with plant, machinery or furniture is let out on hire [Sec. 57(ii)]

Hence no depreciation is allowed in respect of motor car.

Proportionate depreciation on motor car is permissible under the head “business or profession”:

It is assumed it has been allowed as the expression “income from business” refers to taxable income after permissible deductions.

Illustration 3. RP (HUF), furnishes the following particulars of its income and outgoing for the previous year 2011-2012.

Receipts :	4,00,000
(i) Short-term capital gain	1,00,000
(ii) Gross winning from lottery	12,00,000
(iii) Sale consideration of 3/4th of agriculture produce, derived from land located in India, the balance produce has been kept for family use.	50,000
(iv) Net sale proceeds of wild grass and fruits from trees of spontaneous growth	
Payments:	
(i) Repair of tube-well	60,000
WDV of tube-well on 1-4-2011	10,00,000
(ii) Wages paid to agriculture labour	6,00,000
(iii) Manuring and spraying charges	50,000
(iv) Rent of the building, used for storing agriculture produce on site	50,000
(v) Petrol, repair, salary of driver and insurance of motor car.	1,50,000
WDV of motor car on 1-4-2011	2,00,000
50% use of the motor car is for personal purpose of the family	
(vi) LIP paid to insure members of the family	20,000
(vii) School fees paid for 3 children of the family @ ₹ 15,000 per child	45,000
(viii) Purchase of infrastructure bonds, covered under Sec. 80C(2)(xix)	90,000
(ix) Deposit with LIC for maintenance of a dependant member with disability:	
Unabsorbed losses brought forward:	
AY: 2002-2003	40,000
AY: 2004-2005	5,00,000
AY: 2007-2008	1,00,000

Determine the total income of the HUF and its tax liability for the assessment year 2012-2013.



Solution :

Assessee : R P (HUF)

Computation of Total Income: AY 2012-2013

Particulars	₹	₹
Computation of net agriculture income for the purpose of aggregation to determine the rate of tax applicable to non-agriculture income of the HUF.		
Such computation is done under the head business profession:		
(1) Sale proceeds of agriculture produce		12,00,000
Add: Market value of produce kept for family use:		4,00,000
12,00,000 × (4/3) × (1/4)		16,00,000
Less: Permissible deductions:		
(i) Repair of tube-well	60,000	
(ii) Wages	6,00,000	
(iii) Rent	50,000	
(iv) Petrol, repair, salary of driver— 50%	75,000	
(v) Manuring and spraying	50,000	
(vi) Depreciation on tube-well @ 10% on WDV	1,00,000	
(vii) 50% depreciation on motor car: (15% of 2,00,000) × 50%	15,000	9,50,000
Less: Adjustment for Carry Forward Losses :		
(i) Loss 2002-2003-not allowed	Nil	
(ii) Loss from AY 2004-2005	1,00,000	
(iii) Loss from AY 2007-2008	45,000	1,45,000
Net Agriculture Income		5,05,000
(2) Computation of Total Income		
(a) Short-term capital gain		4,00,000
(b) Income from other sources:		
(i) Winnings from lottery	1,00,000	
(ii) Net sale proceeds of non-agriculture produce	50,000	1,50,000
Gross Total Income (excluding Agricultural Income)		5,50,000
Less: Contributions paid for approved savings [Sec. 80C(2)]:		
(i) LIP on the life of members	20,000	
(ii) School fees for 3 children of the HUF [Sec. 80(4)(c)]	Nil	
(iv) Purchase of NSC	90,000	
	1,10,000	
But deduction restricted upto a maximum of ₹1,00,000		1,00,000

2. Deposit for maintenance (including medical treatment) of a dependant with disability (Sec. 80DD)		50,000
Total Non-Agricultural Income		4,00,000
Computation of Tax Liability		
(i) Income tax on winnings 30% on ₹ 1,00,000		30,000
(ii) Income tax on non-agriculture + agriculture income: 3,00,000 + 5,05,000 at slab rates (Non-agricultural income = 3,00,000 = 5,50,000 – 1,00,000 – 1,00,000 – 50,000)		
(a) Income tax on 8,05,000 as if it is the total income	93,500	
(b) Income tax on agriculture income + exemption limit as if it is the total income: 5,05,000 + 1,80,000 = 6,85,000	69,000	
Income tax on non-agriculture income: (a) – (b)		24,500
Tax on total income		54,500
Add:		
(i) Education cess @ 2%		1,090
(ii) SHEC @ 1%		545
Tax payable		56,135

Illustration 4. B Ltd. grows sugarcane to manufacture sugar. The data for the financial year 2011-12 is as follows :

Cost of cultivation of sugarcane	₹ 6,00,000
Market value of sugarcane when transferred to factory	₹ 10,00,000
Other manufacturing cost	₹ 6,00,000
Sales of sugar	₹ 25,00,000
Salary of Managing Director who looks after all operations of the Company	₹ 3,00,000

Solution :

(1) Business Income :

Sales of Sugar	₹ 25,00,000
Less: Market value of sugarcane when transferred to factory	₹ 10,00,000
Other manufacturing cost	₹ 6,00,000
Salary of Managing Director	₹ 3,00,000
	₹ 6,00,000

(2) Agricultural Income :

Market value of sugarcane when transferred to factory	₹ 10,00,000
Less: Cost of cultivation	₹ 6,00,000
	₹ 4,00,000



Illustration 5. Mr. P has estates in Rubber, Tea and Coffee. He has also a nursery wherein he grows plants and sells. For the previous year ending 31.3.2012, he furnishes the following particulars of his sources of income from estates and sale of Plants. You are requested to compute the taxable income for the Assessment year 2012-2013:

Manufacture of Rubber	₹ 5,00,000
Manufacture of Coffee grown and cured	₹ 3,50,000
Manufacture of Tea	₹ 7,00,000
Sale of Plants from Nursery	₹ 1,00,000

Solution :

Computation of Taxable Income

Rule	Nature of Business	Agl Inc.	Non-Agl. Inc.
7A	Sale of centrifuged latex or cenex manufactured from rubber	3,25,000	1,75,000
7B	Sale of grown and cured coffee by seller in India	2,62,500	87,500
8	Growing and Manufacturing Tea	4,20,000	2,80,000
	Sale of plants from nursery	1,00,000	—
	Total	11,07,500	5,42,500

Computation of Tax Liability :

	₹
(a) Total Income (Agricultural Income + Non-agricultural Income)	16,50,000
(b) Tax on (a) above	3,47,000
(c) Total of (Agricultural Income + Basic Exemption Limit)	12,67,500
(d) Tax on (c) above	2,32,250
(e) Tax Payable (b) – (d)	1,47,750
Add: Education Cess @ 2%	2,295
Add: SHEC @ 1%	1,148
Total Tax Liability	1,18,193
Tax payable rounded off u/s 288B	1,18,190

STUDY NOTE - 14

MINIMUM ALTERNATE TAX (MAT)

This Study Note includes

- Provisions under the Income Tax Act relating to Minimum Alternate Tax

14.1 MINIMUM ALTERNATE TAX (MAT) [Sec.115JB]

1. Section 115JB provides that, in the case of a company, if the tax payable on the total income as computed under the Income-tax Act in respect of any previous year is less than Ten per cent of its book profit, such book profit shall be deemed to be the total income of the assessee and the tax payable for the relevant previous year shall be 18.5% of such book profit.
2. The profit and loss account should be prepared in accordance with Parts II and III of Schedule VI of the Companies Act, 1956.

The Accounting Policies, the Accounting Standards adopted for preparing such accounts and the method and rates adopted for calculating the depreciation, shall be the same as have been adopted for the purpose of preparing such accounts and laid before the company at its AGM.

2. "Book Profit" means the net profit as shown in the profit and loss account, as increased by –
 - (a) the amount of income-tax paid or payable, and the provision therefore; or
 - (b) the amounts carried to any reserves, by whatever name called other than a reserve specified under section 33AC; or
 - (c) the amount or amounts set aside to provisions made for meeting liabilities, other than ascertained liabilities; or
 - (d) the amount by way of provision for losses of subsidiary companies; or
 - (e) the amount or amounts of dividends paid or proposed; or
 - (f) the amount or amounts of expenditure relatable to any income to which section 10 [other than the provisions contained in section 10(38) or section 10A or section 10B or section 11 or section 12 apply; or
 - (g) the amount of depreciation if any amount referred to in clauses (a) to (g) is debited to the profit and loss account, and as reduced by –
 - (i) The amount withdrawn from any reserve or provision, if any such amount is credited to the profit and loss account subject to the proviso stated in the section; or
 - (ii) Incomes exempt under any of the provisions of section 10 other than the provisions contained in section 10A [Free Trade Zone Undertaking's income] or 10B [Hundred per Cent Export Oriented Undertaking's income] or section 11 or section 12 [Charitable or religious Trust's income] apply, if any such income is credited to the profit and loss account; or
 - (iii) The amount of depreciation debited to profit and loss account excluding the depreciation on account of revaluation of assets; or
 - (iv) The amount withdrawn from revaluation reserve and credited to profit and loss account, to the extent it does not exceed the amount of depreciation on account of revaluation of assets; or
 - (v) The amount of loss brought forward or unabsorbed depreciation, whichever is less as per books of account.



However, for the purpose of this clause –

- (a) the loss shall not include depreciation;
 - (b) the provisions of this clause shall not apply if the amount of loss brought forward or unabsorbed depreciation is nil; or
 - (vi) The amount of profits of sick industrial company during the years in which such company has become sick industrial company under the provisions of Sick Industrial Companies (Special Provision) Act, 1985.
3. Provisions shall not affect carried forward of depreciation and losses under the applicable provisions mentioned in sub-section (3) of section 115JB.
 4. Profits of an Entrepreneur in SEZ or Developer of SEZ are not liable for MAT.
 5. Tax paid under section 115JB for A.Y. 2006-07 and any subsequent year would be allowed as a credit from the normal tax payable for any subsequent year in accordance with the provisions contained in section 115JAA. However, the amount of tax credit can not be carried forward for set off beyond the seventh assessment year immediately succeeding the assessment year in which tax credit becomes allowable.
 6. A report in prescribed form (Form No. 29B and Rule 40B) from an accountant as defined in the section 288 shall be furnished along with the return of income.
 7. All companies are liable for payment of advance tax having regard to the provisions contained in new section 115JB. Consequently, the provisions of sections 234B and 234C for interest on defaults in payment of advance tax and deferment of advance tax would also be applicable where facts of the case warrant. - Circular : No. 13/2001, dated 9-11-2001.

Rate of Minimum Alternate Tax increased to 18.5% [Section 115JB(1)] [W.e.f. A.Y.2012-13]

Under the existing provisions of section 115JB(1), a company is required to pay a minimum alternate tax (MAT) on its book profit, if the income-tax payable on the total income, as computed under the Act in respect of any previous year relevant to the assessment year commencing on or after 1.4.2011, is less than the MAT. The amount of tax paid under the said section is allowed to be carried forward and set off against tax payable up to the tenth assessment year immediately succeeding the assessment year in which the tax credit becomes allowable under the provisions of section 115JAA.

This section has been amended to increase the rate of MAT to eighteen and one-half per cent from the existing rate of eighteen per cent of such book profit.

Sunset provisions inserted regarding exemption from Minimum Alternate Tax (MAT) and Dividend Distribution Tax (DDT) in case of Special Economic Zones [Sections 115JB(6), 115-O(6) read with section 10AA & 80-IAB]

Under the existing provisions of section 10AA of the Income-tax Act, a deduction of 100% is allowed in respect of profits and gains derived by a unit located in a Special Economic Zone (SEZ) from the export of articles or things or services for the first five consecutive assessment years; of 50% for further five assessment years; and thereafter, of 50% of the ploughed back export profit for the next five years.

Further, under section 80-IAB of the Income-tax Act, a deduction of 100% is allowed in respect of profits and gains derived by an undertaking from the business of development of an SEZ notified on or after 1.4.2005 from the total income for any ten consecutive assessment years out of fifteen years beginning from the year in which the SEZ is notified by the Central Government.

Under the existing provisions of section 115JB(6), an exemption is allowed from payment of minimum alternate tax (MAT) on book profit in respect of the income accrued or arising on or after 1.4.2005 from any business carried on, or services rendered, by an entrepreneur or a Developer, in a Unit or Special Economic Zone (SEZ), as the case may be.

Further, under the existing provisions of section 115-O(6), an exemption is allowed from payment of tax on distributed profits [Dividend Distribution Tax (DDT)] in respect of the total income of an undertaking or enterprise engaged in developing or developing and operating or developing, operating and maintaining a Special Economic Zone for any assessment year on any amount declared, distributed or paid by such Developer or enterprise, by way of dividends (whether interim or otherwise) on or after 1.4.2005 out of its current income. Such distributed income is also exempt from tax under section 10(34) of the Act.

The above provisions were inserted in the Income-tax Act by the Special Economic Zones Act, 2005 (SEZ Act) with effect from 10th February, 2006.

Currently, there is no sunset date provided for exemption from MAT in the case of a developer of an SEZ or a unit located in an SEZ. Similarly, there is no sunset date for exemption from DDT in the case of a developer of an SEZ.

The Finance Act, 2011 has sunset the availability of exemption from minimum alternate tax in the case of SEZ Developers and units in SEZs in the Income-tax Act as well as the SEZ Act w.e.f. A.Y. 2012-13. Hence, units of SEZ and developers of SEZ shall be liable to MAT w.e.f. A.Y. 2012-13.

It has further discontinued the availability of exemption from dividend distribution tax in the case of SEZ Developers under the Income-tax Act as well as the SEZ Act for dividends declared, distributed or paid on or after 1.6.2011 which shall be taxable @ 16.223% (15% + 5% SC + 3% EC + SHEC).

Consequential amendments have also been made by omitting *Explanation* to section 10(34) of the Income-tax Act w.e.f. 1.6.2011.

SPECIAL PROVISIONS RELATING TO CERTAIN LIMITED LIABILITY PARTNERSHIPS (LLP)

Alternate Minimum Tax for Limited Liability Partnership (LLP) [Section 115JC to 115JF] [W.e.f. A.Y. 2012-13]

The Limited Liability Partnership Act, 2008 (LLP) has come into effect in 2009. The LLP has features of both a body corporate as well as a traditional partnership. The Income-tax Act provides for the same taxation regime for a limited liability partnership as is applicable to a partnership firm. It also provides tax neutrality (subject to fulfilment of certain conditions) to conversion of a private limited company or an unlisted public company into an LLP.

An LLP being treated as a firm for taxation, has the following tax advantages over a company under the Income-tax Act :-

- (i) it is not subject to Minimum Alternate Tax;
- (ii) it is not subject to Dividend Distribution Tax (DDT); and
- (iii) it is not subject to surcharge.

In order to preserve the *tax base vis-a-vis profit-linked deductions*, a new Chapter XII-BA has been inserted in the Income-tax Act containing special provisions relating to certain limited liability partnerships.

As per newly inserted Section 115JC, where the regular income-tax payable for a previous year by a limited liability partnership is less than the alternate minimum tax payable for such previous year, the adjusted total income shall be deemed to be the total income of such limited liability partnership and it shall be liable to pay income-tax on such total income at the rate of eighteen and one-half per cent.

Meaning of adjusted total income, alternate minimum tax and regular income-tax [Section 115JF]

- (i) "adjusted total income" shall be the total income before giving effect to this newly inserted Chapter XII-BA as increased by the deductions claimed under any section included in Chapter VI-A under the heading "C-Deductions in respect of certain incomes" and deduction claimed under section 10AA;
- (ii) "alternate minimum tax" shall be the amount of tax computed on adjusted total income at a rate of eighteen and one-half per cent; and
- (iii) "regular income-tax" shall be the income-tax payable for a previous year by a limited liability partnership on its total income in accordance with the provisions of the Act other than the provisions of this newly inserted Chapter XII-BA.

Tax credit for alternate minimum tax [Section 115JD] : The credit for tax (tax credit) paid by a limited liability partnership under this newly inserted Chapter XII-BA shall be allowed to the extent of the excess of the alternate minimum tax paid over the regular income-tax. This tax credit shall be allowed to be carried forward up to the tenth assessment year immediately succeeding the assessment year for which such credit becomes allowable. It shall be allowed to be set off for an assessment year in which the regular income-tax exceeds the alternate minimum tax to the extent of the excess of the regular income-tax over the alternate minimum tax.

Application of other provisions of this Act [Section 115JE] : Save as otherwise provided in this Chapter, all other provisions of this Act shall apply to a limited liability partnership referred to in this Chapter. Hence, all other provisions relating to Advance tax, interest under sections 234A, 234B and 234C penalty, etc. shall apply to such Limited Liability Partnership also.

Illustration : The following is the profit and loss account for the year ending 31.3.2012 of XYZ (LLP) having 3 partners :

Profit and Loss Account

		₹		₹
Establishment & other expenses		48,00,000	Gross profit	68,20,000
Interest to partner @ 15%			Profit on sales of equity shares sold after	
X	90,000		2 years through recognised stock exchange	1,40,000
Y	1,20,000			
Z	60,000	2,70,000		
Salary to designated partners			Rent from house property	60,000
X	2,40,000		Interest on bank deposits	10,000
Y	1,80,000	4,20,000	Profit on equity shares sold after	
Net profit		17,60,000	10 months through RSE	1,20,000
		<u>72,50,000</u>		<u>72,50,000</u>

Additional information :

- (1) Establishment expenses include ₹ 1,20,000 on account of bonus which was due on 31.3.2012.
- (2) The LLP is eligible for 100% deduction under section 80-IC as it is established in notified area in Himachal Pradesh.
- (3) Shares were sold through recognized stock exchange and securities transaction tax of ₹ 1000 is included in the establishment expenses on account of the same.

Compute the tax payable by the Limited Liability Firm

Solution :

Computation of total income of XYZ (LLP) for the A.Y. 2012-13

<i>Income under the head house property</i>	₹	₹	₹
Actual rent		1,60,000	
Less : Deduction 30%		<u>48,000</u>	1,12,000
<i>Business income</i>			
Net profit as per P&L A/c		16,60,000	
Less : Income credited but either exempt or taxable under other head			
Rent	60,000		
Profit on sale of shares sold after 2 years	1,40,000		
Interest on bank deposit	10,000		
Profit on sale of shares sold after 10 months	<u>1,20,000</u>	<u>3,30,000</u>	
		13,30,000	
<i>Add : Expenses disallowed</i>			
Bonus as per section 43B	1,20,000		
Securities Transaction Tax	1,000		
Interest to partners in excess of 12%	54,000		
Salary to partners	<u>4,20,000</u>	<u>5,95,000</u>	
Book profit		19,25,000	
Less : Salary as per section 40(b) (See working note)		<u>4,20,000</u>	15,05,000
Short-term capital gain on sale of equity shares			1,20,000
Income from other sources			<u>10,000</u>
Gross total income			17,47,000
Less : Deduction under section 80-IC			<u>15,05,000</u>
Total income			2,42,000

Regular income tax payable on total income

(1) Short-term capital gain of ₹ 1,20,000 @ 15%	18,000
(2) Balance total income ₹ 1,22,000 @ 30%	36,600
	<u>54,600</u>

Adjusted total income

Total income	2,42,000
Add : Deduction u/s Chapter VIA	<u>15,05,000</u>
	<u>17,47,000</u>

Alternate Minimum Tax (AMT) 18.5% on ₹ 17,47,000 = ₹ 3,23,195

Hence, adjusted total income shall be total income and the tax (payable shall be the alternate minimum tax i.e. on ₹ 17,47,000 @ 18.5% + 3% (EC + SHEC).

Tax payable

	₹
Alternate minimum tax 18.5% on ₹ 17,47,000	3,23,195
Add : 3% Education cess & SHEC	<u>9,696</u>
	<u>3,32,891</u>
Rounded off	<u>3,32,890</u>

Working Note

Book profit	19,25,000
Maximum salary allowed	
First 3,00,000 of book profit — 90%	2,70,000
Balance ₹ 16,25,000 of book profit 60%	<u>9,75,000</u>
	<u>12,45,000</u>

Salary allowed shall be ₹ 12,45,000 or ₹ 4,20,000 whichever is lower i.e. ₹ 4,20,000.

ILLUSTRATIONS ON MINIMUM ALTERNATE TAX

Illustration 1. D Ltd., a closely-held Indian company, is engaged in the business of manufacture of chemical goods (value of plant and machinery owned by the company is ₹ 55 lakh). The following informations for the financial year 2011-12 are given :

D Ltd. is engaged in the business of manufacture of garments.

	₹
Sale proceeds of goods (domestic sale)	25,00,000
Sale proceeds of goods (export sale)	7,00,000
Amount withdrawn from general reserve (reserve was created in 1997-98 by debiting P&L A/c)	2,00,000
Amount withdrawn from revaluation reserve	1,50,000
Total	35,50,000
Less : Expenses	
Depreciation (normal)	6,16,000
Depreciation (extra depreciation because of revaluation)	2,70,000
Salary and wages	2,10,000
Wealth tax	10,000
Income-tax	3,50,000
Outstanding customs duty (not paid as yet)	17,500
Proposed dividend	60,000
Consultation fees paid to tax expert	21,000
Other expenses	1,39,000
Net Profit	18,56,500

For tax purposes the company wants to claim the following :

- Deduction under section 80-1B (30 per cent of ₹ 14,56,500).
- Depreciation under section 32 (₹ 5,36,000)

The company wants to set off the following losses/allowances :

	For tax purposes ₹	For accounting purposes ₹
Brought forward loss of 2004-05	14,80,000	4,00,000
Unabsorbed depreciation	—	70,000

Compute the net income and tax liability of D Ltd. for the assessment year 2012-13 assuming that D Ltd. has a (deemed) long-term capital gain of ₹ 60,000 under proviso (i) to section 54D(2) which is not credited in profit and loss account.

Solution :

Computation of Book Profit & Minimum Alternate Tax

	₹
Net profit as per P&L A/c	18,56,500
Add :	
Excess depreciation [i.e., ₹ 6,16,000 + ₹ 2,70,000 — ₹ 5,36,000]	3,50,000
Wealth tax	10,000
Income tax	3,50,000
Customs duty which is not paid	17,500
Proposed dividend	60,000
Total	26,44,000
Less : Amount withdrawn from reserve (i.e., ₹ 2,00,000+₹ 1,50,000)	3,50,000
Business income	22,94,000
Less : Unabsorbed loss	14,80,000
Business Income	8,14,000
Long-term capital gain	60,000
Gross total income	8,74,000
Less : Deductions under section 80-IB [30% of ₹ 4,14,000]	1,24,200
Net Income (rounded off)	7,49,800
Tax liability (under normal provisions) [20% of ₹ 60,000 + 30% of ₹ 6,89,800, plus 3% of tax as cess]	2,25,508
Book profit	
Net Profit	18,56,500
Add :	
Depreciation (i.e. ₹ 6,16,000 + ₹ 2,70,000)	8,86,000
Wealth tax	Nil
Income-tax	3,50,000
Proposed dividend	60,000
Less : Amount withdrawn from general reserve	(–) 2,00,000
Unabsorbed depreciation	(–) 70,000
Depreciation (normal)	(–) 6,16,000
Amount withdrawn from revaluation reserve to the extent it does not exceed extra depreciation because of revaluation	(–) 1,50,000
Book profit	21,16,500
Tax liability (19.055% of 21,16,500)	4,03,299

D Ltd. will pay ₹ 4,03,299 as tax for the assessment year 2012-13 as per section 115JB. Tax credit is however, available in respect excess tax (i.e., ₹ 1,77,791) under section 115JB.



STUDY NOTE - 15

RETURN OF INCOME

This Study Note includes

- Different Provisions relating to Return of Income

15.1 RETURN OF INCOME

The starting point for assessment of income is furnishing of return of income. Filing of return of income is mandatory for certain category of assessee. Incidental provisions for accompaniments to the return of income, error correction, belated returns have been made. Now filing of the return electronically has been made mandatory for certain category of assessee.

Return of income is the format in which the assessee has to furnish information as to his total income and tax payable. The format for filing of returns by different assessee is notified by the CBDT.

COMPULSORY FILING OF RETURN OF INCOME [SECTION 139(1)]

- (1) As per section 139(1), it is compulsory for companies and firms to file a return of income for every previous year.
- (2) In case of a person other than a company or a firm, filing of return of income is mandatory, if his total income or the total income of any other person in respect of which he is assessable under this Act during the previous year exceeds the basic exemption limit.
- (3) Such persons should, on or before the due date, furnish a return of income in the prescribed form and verified in the prescribed manner and setting forth such other particulars as may be prescribed.
- (4) Further, every person, being an individual or a HUF or an AOP or BOI or an artificial juridical person—

– whose total income or the total income of any other person in respect of which he is assessable under this Act during the previous year

– without giving effect to the provisions of section 10A or 10B or 10BA or Chapter VI-A - exceeded the basic exemption limit is required to file a return of his income or income of such other person—

(5) For company and certain other assessee like firm having tax audit, filing of return in an electronic form is mandatory. (Section 139D)

'Due date' means -

- 30th September of the assessment year, where the assessee is -*
 - a company; or*
 - a person (other than a company) whose accounts are required to be audited under the Income-tax Act, 1961 or any other law in force; or*
 - a working partner of a firm whose accounts are required to be audited under the Income-tax Act, 1961 or any other law for the time being in force.*
- 31st July of the assessment year, in the case of any assessee other than those covered in (a) above.*

INTEREST FOR DEFAULT IN FURNISHING RETURN OF INCOME [SECTION 234A]

- (1) Interest under section 234A is attracted where an assessee furnishes the return of income after the due date or does not furnish the return of income.
- (2) The interest is payable for the period commencing from the date immediately following the due date and ending on the following dates -
When the return is furnished after due date : the date of furnishing of the return
Where no return is furnished : the date of completion of assessment
- (3) The interest has to be calculated on the amount of tax on total income as determined under section 143(1) or on regular assessment as reduced by the advance tax paid and any tax deducted or collected at source.

OPTION TO FURNISH RETURN OF INCOME TO EMPLOYER [SECTION 139(1A)]

- (1) This section gives an option to a person, being an individual who is in receipt of income chargeable under the head "Salaries", to furnish a return of his income for any previous year to his employer, in accordance with such scheme as may be notified by the CBDT and subject to such conditions as may be specified therein.
- (2) Such employer shall furnish all returns of income received by him on or before the due date, in such form, including on a floppy, diskette, magnetic cartridge tape, CD-ROM or any other computer readable media and manner as may be specified in that scheme.
- (3) In such a case, any employee who has filed a return of his income to his employer shall be deemed to have furnished a return of income under sub-section (1).

INCOME-TAX RETURN THROUGH COMPUTER READABLE MEDIA [SECTION 139(1B)]

- (1) This sub-section enables the taxpayer to file his return of income in computer readable media, without interface with the department.
- (2) Such person may, on or before the due date, furnish a return of income in accordance with such scheme as may be notified by the CBDT, in such form, including on a floppy, diskette, magnetic cartridge tape, CD-ROM or any other computer readable media and manner as may be specified in that scheme.

RETURN OF LOSS [SECTION 139(3)]

- (1) This section requires the assessee to file a return of loss in the same manner as in the case of return of income within the time allowed under section 139(1).
- (2) Under section 80, an assessee cannot carry forward or set off his loss against income in the same or subsequent year unless he has filed a return of loss in accordance with the provisions of section 139(3).
- (3) A return of loss has to be filed by the assessee in his own interest and the non-receipt of a notice from the Assessing Officer requiring him to file the return cannot be a valid excuse under any circumstances for the non-filing of such return.
- (4) In particular, a return of loss must be filed by an assessee who has incurred a loss under the heads "profits and gains from business or profession", "capital gains", and income from the activity of owning and maintaining race horses taxable under the head "Income from other sources".
- (5) *However, loss under the head "Income from house property" under section 71B and unabsorbed depreciation under section 32 can be carried forward for set-off even though return of loss has not been filed before the due date.*

BELETED RETURN [SECTION 139(4)]

- (1) Any person who has not furnished a return within the time allowed to him under section 139(1) or within the time allowed under a notice issued under section 142(1) may furnish the return for any previous year at any time -
 - (i) before the expiry of one year from the end of the relevant assessment year; or
 - (ii) before the completion of the assessment, whichever is earlier.
- (2) Interest is required to be paid under section 234A, as stated above.

**RETURN OF INCOME OF CHARITABLE TRUSTS AND INSTITUTIONS [SECTION 139(4A)]**

- (1) Every person in receipt of income –
 - (i) derived from property held under a trust or any other legal obligation wholly or partly for charitable or religious purpose; or
 - (ii) by way of voluntary contributions on behalf of such trust or institution must furnish a return of income if the total income in respect of which he is assessable as a representative assessee, computed before allowing any exemption under sections 11 and 12 exceeds the basic exemption limit.
- (2) Such persons should furnish the return in the prescribed form and verified in the prescribed manner containing all the particulars prescribed for this purpose.
- (3) This return must be filed by the representative-assessee voluntarily within the time limit. Any failure on the part of the assessee would attract liability to pay interest and penalty.

RETURN OF INCOME OF POLITICAL PARTIES [SECTION 139(4B)]

- (1) Under this section, a political party is required to file a return of income if, before claiming exemption under section 13A, the party has taxable income.
- (2) The grant of exemption from income-tax to any political party under section 13A is subject to the condition that the political party submits a return of its total income within the time limit prescribed under section 139(1).
- (3) The chief executive officer of the political party is statutorily required to furnish a return of income of the party for the relevant assessment year, if the amount of total income of the previous year exceeds the basic exemption limit before claiming exemption under section 13A.

REVISED RETURN [SECTION 139(5)]

- (1) If any person having furnished a return under section 139(1) or in pursuance of a notice issued under section 142(1), discovers any omission or any wrong statement therein, he may furnish a revised return at any time before the expiry of one year from the end of the relevant assessment year or before completion of assessment, whichever is earlier.
- (2) It may be noted that a belated return cannot be revised. It has been held in *Kumar Jagdish Chandra Sinha v. CIT* [1996] 86 Taxman 122 (SC) that only a return furnished under section 139(1) or in pursuance of a notice under section 142(1) can be revised. A belated return furnished under section 139(4), therefore, cannot be revised.

PARTICULARS REQUIRED TO BE FURNISHED WITH THE RETURN [SECTION 139(6)]

The prescribed form of the return shall, in certain specified cases, require the assessee to furnish the particulars of -

- (i) income exempt from tax
- (ii) assets of the prescribed nature and value and belonging to him
- (iii) his bank account and credit card held by him
- (iv) expenditure exceeding the prescribed limits incurred by him under prescribed heads
- (v) such other outgoings as may be prescribed.

DEFECTIVE RETURN [SECTION 139(9)]

- (1) Under this sub-section, the Assessing Officer has the power to call upon the assessee to rectify a defective return.
- (2) Where the Assessing Officer considers that the return of income furnished by the assessee is defective, he may intimate the defect to the assessee and give him an opportunity to rectify the defect within a period of 15 days from the date of such intimation. The Assessing Officer has the discretion to extend the time period beyond 15 days, on an application made by the assessee.

- (3) If the defect is not rectified within the period of 15 days or such further extended period, then the return would be treated as an invalid return. The consequential effect would be the same as if the assessee had failed to furnish the return.
- (4) Where, however, the assessee rectifies the defect after the expiry of the period of 15 days or the further extended period, but before assessment is made, the Assessing Officer can condone the delay and treat the return as a valid return.
- (5) A return can be treated as defective if it is not properly filled in or the necessary enclosures are not accompanying the return.

Specific defects are only illustrative and not exhaustive - CIT v. Rai Bahadur Bissesswarlal Motilal Malwasie Trust 195 ITR 825.

SCHEME FOR SUBMISSION OF RETURNS THROUGH TAX RETURN PREPARERS [SECTION 139B]

- (1) The Tax Return Preparer shall assist the persons furnishing the return in a manner that will be specified in the Scheme, and shall also affix his signature on such return. The “specified class or classes of persons” for this purpose means any person other than a company or a person whose accounts are required to be audited under section 44AB (tax audit) or under any other existing law, who is required to furnish a return of income under the Act.
- (2) A Tax Return Preparer can be an individual, other than
 - (i) any officer of a scheduled bank with which the assessee maintains a current account or has other regular dealings.
 - (ii) any legal practitioner who is entitled to practice in any civil court in India.
 - (iii) a chartered accountant.
 - (iv) an employee of the ‘specified class or classes of persons’.
- (3) The Scheme notified under the said section may provide for the following —
 - (i) the manner in which and the period for which the Tax Return Preparers shall be authorised,
 - (ii) the educational and other qualifications to be possessed, and the training and other conditions required to be fulfilled, by a person to act as a Tax Return Preparer,
 - (iii) the code of conduct for the Tax Return Preparers,
 - (iv) the duties and obligations of the Tax Return Preparers,
 - (v) the circumstances under which the authorisation given to a Tax Return Preparer may be withdrawn, and
 - (vi) any other relevant matter as may be specified by the Scheme.

PERMANENT ACCOUNT NUMBER (PAN) [SECTION 139A]

- (1) Where any person in the following category has not been allotted a permanent account number (PAN), he should apply to the Assessing Officer within the prescribed time for allotment of a PAN -
 - (i) Every person whose total income or the total income of any other person in respect of which he is assessable under this Act during any previous year exceeded the basic exemption limit; or
 - (ii) Every person carrying on any business or profession whose total sales, turnover or gross receipts exceeds or is likely to exceed ₹5 lakhs in any previous year; or
 - (iii) Every person who is required to furnish a return of income under section 139(4A); or
 - (iv) Every person, being an employer, who is required to furnish a return of fringe benefits under section 115WD [Sub-section (1)].
- (2) The CBDT had introduced a new scheme of allotment of computerized 10 digit PAN. Such PAN comprises of 10 alphanumeric characters and is issued in the form of a laminated card.
- (3) All persons who were allotted PAN (Old PAN) earlier and all those persons who were not so allotted but were required to apply for PAN, shall apply to the Assessing Officer for a new series PAN within specified time.



- (4) Once the new series PAN is allotted to any person, the old PAN shall cease to have effect. No person who has obtained the new series PAN shall apply, obtain or process another PAN.
- (5) On receipt of allotment of PAN it must be mentioned on all tax payment challans, returns, correspondence.
- (6) Where TDS or TCS is made, the person from whom it is made must communicate his PAN to the person deducting or collecting tax.
- (7) Every person receiving any document relating to a transaction prescribed under clause (c) of sub-section (5) shall ensure that the permanent account number or the General Index Register Number has been duly quoted in the document.

Power of Board to dispense with furnishing documents, etc. with the return [Sec. 139C]

- (1) The Board may make rules providing for a class or classes of persons who may not be required to furnish documents, statements, receipts, certificates, reports of audit or any other documents, which are otherwise under any other provisions of this Act, except section 139D, required to be furnished, along with the return but on demand to be produced before the Assessing Officer.
- (2) Any rule made under the proviso to sub-section (9) of section 139 as it stood immediately before its omission by the Finance Act, 2007 shall be deemed to have **been made under the provisions of this section.**

Filing of return in electronic form [Sec. 139D] : The Board may make rules providing for—

- (a) the class or classes of persons who shall be required to furnish the return in electronic form;
- (b) the form and the manner in which the return in electronic form may be furnished;
- (c) the documents, statements, receipts, certificates or audited reports which may not be furnished along with the return in electronic form but shall be produced before the Assessing Officer on demand;
- (d) the computer resource or the electronic record to which the return in electronic form may be transmitted.

RETURN BY WHOM TO BE SIGNED [Section 140]

The return under **section 115WD** or **section 139** shall be signed and verified as under:

Sr. No.	Assessee Category	Who can Sign
1	Individual	(i) by the individual himself; (ii) where he is absent from India, by the individual himself or by some person duly authorised by him in this behalf; (iii) where he is mentally incapacitated from attending to his affairs, by his guardian or any other person competent to act on his behalf; and (iv) where, for any other reason, it is not possible for the individual to sign the return, by any person duly authorised by him in this behalf.
2	Hindu Undivided Family (HUF)	by the Karta and where the karta is absent from India or is mentally incapacitated from attending to his affairs, by any other adult member of such family
3	Company	Managing director or where for any unavoidable reason managing director is not able to sign or where there is no managing director, by any director thereof. Exceptions : (a) where the company is being wound up : by the liquidator (b) where the management of the company has been taken over by the Government : the principal officer thereof (c) company is not resident in India : a person who holds a valid power of attorney
4	A Firm / Limited Liability Partnership (w.e.f. A.Y 2010-11)	Managing partner or where for any unavoidable reason managing partner is not able to sign and verify the return, or where there is no managing partner, by any partner thereof
5	A Local Authority	The Principal officer thereof

Sr. No.	Assessee Category	Who can Sign
6	A Political Party	The Chief Executive Officer of such party
7	Any other Association	any Member of the Association or the Principal Officer thereof
8	Any other Person	by that person or by some person competent to act on his behalf

Prescribed Forms :

Forms	Applicability
ITR - 1	Return of Income for Individuals having salary and interest income and no other Income
ITR-2	Return of income for Individuals and HUFs having income from any source except from business or profession
ITR-3	Return of income for Individuals and HUFs being partners in Firms and not having Proprietary business or profession
ITR -4	Return of Income for Individuals and HUFs having Proprietary business or profession
ITR-5	Combined form of Return of Income and Fringe Benefits for Firms/ AOP/BOI.
ITR-6	Combined Form for Return of Income and Fringe Benefits for Companies
ITR-7	Combined Form For Return of Income and Fringe Benefits For Charitable/Religious Trusts, Political parties and other Non-Profit Organisations
ITR-8	Stand alone form for Return of Fringe Benefits for persons who are not liable to file Return of income but are liable to file Return of Fringe-Benefits
ITR-V	Return of Income/Fringe Benefits transmitted electronically without digital signatures

SELF-ASSESSMENT TAX PAYMENT [Section 140A]

- (1) Where any tax is payable on the basis of any return required to be furnished under section 115WD or section 115WH or section 139 or section 142 or section 148 or section 153A or, as the case may be, section 158BC, after taking into account taxes paid earlier the assessee shall be liable to pay such tax together with interest payable under any provision of this Act for any delay in furnishing the return or any default or delay in payment of advance tax, before furnishing the return and the return shall be accompanied by proof of payment of such tax and interest.
- (2) If assessee fails to pay the whole or any part of such tax or interest or both on self assessment, he shall be deemed to be an assessee in default in respect of the tax or interest or both remaining unpaid. Penalty can be imposed on any assessee who is in default.

QUESTIONS & ANSWERS ON RETURN OF INCOME

Question 1. What is the due date of filling of return of income in case of a non-working partner of a firm whose accounts are not liable to be audited?

Answer : Due date of furnishing return of income in case of non-working partner shall be 31st July of the assessment year whether the accounts of the firm are required to be audited or not.

A working partner for the above purpose shall mean an individual who is actively engaged in conducting the affairs of the business or profession of the firm of which he is a partner and is drawing remuneration from the firm.

Question 2. What do you mean by annexure less return? What is the manner of filling the return of income?

Answer : The return of income and return of fringe benefits required to be furnished in Form No. ITR-1, ITR-2, ITR-3, ITR-4, ITR-5, ITR-6 or ITR-8 shall not be accompanied by a statement showing the computation of the tax payable on the basis of the return, or proof of the tax, if any, claimed to have been deducted or collected at source or the



advance tax or tax on self-assessment, if any, claimed to have been paid or any document or copy of any account or Form or report of audit required to be attached with the return of income or the return of fringe benefits under any of the provisions of the Act.

Manner of filling the return: The return of income or return of fringe benefits referred to in sub-rule (1) may be furnished in any of the following manners, namely:-

- (i) Furnishing the return in a paper form;
- (ii) Furnishing the return electronically under digital signature;
- (iii) Transmitting the data in the return electronically and thereafter submitting the verification of the return in Form ITR-V;
- (iv) Furnishing a bar-coded return in paper form.

Question 3. Is e-filling of return mandatory? State the assessee's for whom e-filling of returns is mandatory?

Answer : It shall be mandatory for the following assessee's to file the return electronically:

- (a) A firm required to furnish the return in Form ITR-5 and to whom provisions of Section.44AB are applicable, or
- (b) A company required to furnish the return in Form ITR-6

Question 4. Can unabsorbed depreciation be carried forward even if the return is filed after due date?

Answer : Unabsorbed depreciation can be carried forward even if the return of loss is submitted after the due date, as it is not covered under Chapter VI of set off or carry forward of losses but covered u/s 32(2). [East Asiatic Co.(India) Pvt. Ltd. vs.CIT (1986) 161 ITR 135(Mad.)]

Question 5. Can a belated return of income filed u/s 139(4) be revised?

Answer : There was a difference of opinion among various courts regarding filling of revised return in respect of belated returns. However, it has been held that a belated return filed u/s 139(4) cannot be revised as section 139(5) provides that only return filed u/s 139(1) or in pursuance to a notice u/s 142(1) can be revised [Kumar Jagdish Chandra Sinha vs.CIT(1996) 220 ITR 67(SC)].

Question 6. Can a revised return be further revised?

Answer : If the assessee discovers any omission or any wrong statement in a revised return, it is possible to revise such a revised return provided it is revised within the same prescribed time [Niranjan Lal Ram Chandra Vs.CIT (1982) 134 ITR 352 (All.)]

Question 7. Can an Assessing Officer himself allot permanent account number to an assessee?

Answer: The Assessing Officer having regard to the nature of the transactions as may be prescribed may also allot a permanent account number to any other person(whether any tax is payable by him or not) in the manner and in accordance with the procedure as may be prescribed.

Question 8. What are the consequences if a person fails to comply with the provisions of Sec.139A i.e. quoting of PAN?

Answer : As per Sec.272B(2), if a person fails to comply with the provisions of Sec.139A, the Assessing Officer may direct that such person shall have to pay, by way of penalty, a sum of ₹10,000.

Question 9. Who can sign the return of HUF, if HUF does not have a major member?

Answer : If the HUF has no major members as its Karta, a return may validly be signed by the eldest minor member of the family who manages the affairs of the family [Sridhar Udai Narayan Vs.CIT(1962) 45 ITR 577 (All.)]

Question 10. Is thumb impression valid for furnishing the Return of Income?

Answer : The General Clauses Act accepts the thumb impression, as one of the modes of signing, valid and binding. [CIT vs. Kanhaiya Lal And Sons (2005) 273 ITR 425 (All.)]

STUDY NOTE - 16

ASSESSMENT PROCEDURE

This Study Note includes

- Different Provisions relating to Assessment Procedure

16.1 ASSESSMENT PROCEDURE

Inquiry before assessment. [Section 142]

Inquiry :

- (1) The Assessing Officer has power to make inquiry from any person (a) who has made a return under section 139 or (b) in whose case the time allowed under section 139(1) for furnishing the return has expired. For the purpose a notice can be issued for :
 - (i) where such person has not made a return within the time allowed under section 139(1), to furnish a return of his income or
 - (ii) to produce such accounts or documents as the Assessing Officer may require, or
 - (iii) to furnish in writing and verified in the prescribed manner information in such form and on such points or matters including a statement of all assets and liabilities of the assessee, whether included in the accounts or not, as the Assessing Officer may require:
- (2) For the purpose of obtaining full information in respect of the income or loss of any person, the Assessing Officer may make such inquiry as he considers necessary.

Audit :

If the Assessing Officer, having regard to the nature and complexity of the accounts of the assessee and the interests of the revenue, opines that it is necessary so to do, he may, direct the assessee to get the accounts audited by an accountant, as defined in the *Explanation* below section 288(2) and to furnish an audit report, within such period as may be specified, in the prescribed form. The expenses of such audit shall be paid by the assessee

These provisions of audit shall have effect notwithstanding that the accounts of the assessee have been already audited.

Opportunity to Assessee :

The assessee shall be given an opportunity of being heard in respect of any material gathered on the basis of any inquiry or any audit and proposed to be utilised for the purposes of the assessment. Such opportunity need not be given where the assessment is made under section 144.

Estimate by Valuation Officer in certain cases [Sec. 142A]

For the purposes of making an assessment under this Act, where an estimate of the value of any investment referred to in section 69 or section 69B or the value of any bullion, jewellery or other valuable article referred to in section 69A or section 69B is required to be made, the Assessing Officer may require the Valuation Officer to make an estimate of such value and report the same to him.

On receipt of the report from the Valuation Officer, the Assessing Officer may, after giving the assessee an opportunity of being heard, take into account such report in making such assessment:

Case Law :

Assessing Officer can look into documents other than books of account for issuing directions - Submission of audited accounts per se would not oust the jurisdiction of the Assessing Officer to pass a direction for special audit. While



applying his mind, the Assessing Officer need not confine himself only to the books of account submitted by the assessee, but can take into consideration such other documents related thereto which would be part of the assessment proceedings - *Rajesh Kumar Ors. v. Dy. CIT*. 287 ITR 91.

ASSESSMENT [Section 143]

Intimation [Section 143(1)]

Where a return has been made under section 139, or in response to a notice under sub-section (1) of section 142, on the basis of such a return —

- (i) if any tax or interest is found due, after reducing TDS, TCS, advance tax, any self-assessment tax or any other amount paid, then an intimation shall be sent to the assessee specifying the sum so payable, and
- (ii) if any refund is due to the assessee, it shall be granted to him and an intimation to this effect shall be sent to him

In all other cases i.e. where tax paid is equal to tax payable, acknowledgement of the return shall be deemed to be an intimation.

Intimation shall not be sent after the expiry of one year from the end of the financial year in which the return is made.

Power under section 143(1B) extended by one year due to delay in Centralized Processing of Returns.

The Income-tax department is in the process of setting up a Centralised Processing Centre (CPC) at Bengaluru for centralised processing of Income tax and Fringe benefits tax returns. For this purpose the Board had been empowered to relax, modify or adapt any provision of law relating to processing of returns subject to the condition that the notification for such relaxation, modification or adaptation is issued on or before 31-3-2009 and the said notification is laid on the table of the House. Since the centre has still not been operationalised, it is necessary to allow the Board a further period of one year i.e. up to 31-3-2010 to relax, modify or adapt any provision of law relating to processing of returns.

Regular Assessment [Section 143(3)]

Where a return has been furnished under section 139, or in response to a notice under sub-section (1) of section 142, the Assessing Officer shall, if he considers it necessary or expedient to ensure that the assessee has not understated the income or has not computed excessive loss or has not under-paid the tax in any manner, serve on the assessee a notice requiring him, either to attend his office or to produce, any evidence on which the assessee may rely in support of the return. However, no notice shall be served after the expiry of twelve months from the end of the month in which the return is furnished.

On the day specified in the notice issued or as soon afterwards as may be, after hearing such evidence as the assessee may produce and such other evidence as the Assessing Officer may require on specified points, and after taking into account all relevant material which he has gathered, the Assessing Officer shall, by an order in writing, make an assessment of the total income or loss of the assessee, and determine the sum payable by him or refund of any amount due to him on the basis of such assessment.

Tax has to be determined and such determination is to be made in the Asst. order or computation sheet to be annexed with the Asst. order. [*Kalyan Kumar Ray vs. CIT*]

The assessed income may be lower than the returned income. The boards circular no 549 para 5.12 dt. 31.10.1989 has been held to be ultra-vires *Gujarat Gas Co Ltd v JCIT(A)*

Best Judgement Assessment [Section 144]

Best judgement assessment that is popularly known as ex-parte assessment can be made if the assessee fails to comply with the requirement of law as following :-

- (1) The assessee fails to file a return U/s 139 or
- (2) He fails to comply with the terms of the notice issued U/s 142(1) or fails to comply with a direction issued U/s 142(2A).
- (3) After filing a return he fails to comply with all the terms of the notice issued u/s 143(2).

The non-compliances are independent and not cumulative. A single non compliance can lead to best judgement u/s 144. In such a situation the A.O. after taking into account all relevant materials which he has gathered and after giving the assessee an opportunity of being heard shall make an assessment of income or loss to the best of his judgement and determine the sum payable by him. There is no provision for granting refund u/s 144. Provision for granting refund has been withdrawn with effect from 1.4.88. However, where a notice u/s 142(1) has already been issued to the assessee it will not be necessary to give him such opportunity of being heard.

Best judgement asst. is mandatory for any one of the defaults u/s 144 - CIT vs Segn. Buchiah Sethy [1970] 77 ITR 539 (SC).

Where Assessing Officer, on finding that assessee had not maintained and kept any quantitative details/stock register for goods traded in by it; that there was no evidence on record or document to verify basis of valuation of closing stock shown by assessee; and that GP rate declared by assessee during assessment year did not match result declared by assessee itself in previous assessment years, rejected assessee's books of account and resorted to best judgment assessment under section 144, it was held that since cogent reasons had been given by Assessing Officer for doing so, there was no reason to take a different view - Kachwala Gems v. Jt. CIT 158 Taxman 71.

The assessments made on the basis of the assessee's accounts and those made on 'best judgment' basis are totally different types of assessments - CST v. H.M. Esufali H.M. Abdulai 90 ITR 271.

The mere fact that the material placed by the assessee before the assessing officer is unreliable does not empower the officer to make an arbitrary order. The power to make a best judgment assessment is not an arbitrary power - State of Orissa v. Maharaja Shri B.P. Singh Deo 76 ITR 690.

The authority making a best judgment assessment must make an honest and fair estimate of the income of the assessee and though arbitrariness cannot be avoided in such an estimate, the same must not be capricious but should have a reasonable nexus to the available material and the circumstances of the case - Brij Bhushan Lal Parduman Kumar v. CIT 115 ITR 524.

Power of Joint Commissioner to issue directions in certain cases [Sec. 144A]

A Joint Commissioner may, on his own motion or on a reference being made to him by the Assessing Officer or on the application of an assessee, call for and examine the record of any proceeding in which an assessment is pending and, if he considers that, having regard to the nature of the case or the amount involved or for any other reason, it is necessary or expedient so to do, he may issue such directions as he thinks fit for the guidance of the Assessing Officer to enable him to complete the assessment and such directions shall be binding on the Assessing Officer :

Provided that no directions which are prejudicial to the assessee shall be issued before an opportunity is given to the assessee to be heard.

Provision for constitution of alternate dispute resolution mechanism for order of the Transfer Pricing Officer, and foreign company (Section 144C) (W.e.f. 1-10-2009)

The dispute resolution mechanism presently in place is time consuming and finality in high demand cases is attained only after a long drawn litigation till Supreme Court. Flow of foreign investment is extremely sensitive to prolonged uncertainty in tax related matter. Therefore, the Act has amended the Income-tax Act to provide for an alternate dispute resolution mechanism, which will facilitate expeditious resolution of disputes in a fast track basis.

The salient features of the alternate dispute resolution mechanism are as under:—

1. The Assessing Officer shall, forward a draft of the proposed order of assessment (hereinafter in this section referred to as the draft order) to the eligible assessee if he proposes to make, on or after 1-10-2009, any variation in the income or loss returned which is prejudicial to the interest of such assessee.
2. On receipt of the draft order, the eligible assessee shall, within thirty days of the receipt by him of the draft order,
 - (a) File his acceptance of the variations to the Assessing Officer; or
 - (b) File his objections, if any, to such variation with,—
 - (i) The Dispute Resolution Panel; and
 - (ii) The Assessing Officer.



3. The Assessing Officer shall complete the assessment on the basis of the draft order, if—
 - (a) The assessee intimates to the Assessing Officer the acceptance of the variation; or
 - (b) No objections are received within the period specified in sub-section (2) i.e. 30 days of the receipts of draft order by the eligible assessee.
4. The Assessing Officer shall, notwithstanding anything contained in section 153, pass the assessment order under section 144C(3) within one month from the end of the month in which,—
 - (a) The acceptance is received; or
 - (b) The period of filing of objections under sub-section (2) expires.
5. The Dispute Resolution Panel shall, in a case where any objections are received under sub-section (2), issue such directions, as it thinks fit, for the guidance of the Assessing Officer to enable him to complete the assessment.
6. The Dispute Resolution Panel shall issue the directions referred to in sub-section (5), after considering the following, namely:—
 - (a) Draft order;
 - (b) Objections filed by the assessee;
 - (c) Evidence furnished by the assessee;
 - (d) Report, if any, of the Assessing Officer, Valuation Officer or Transfer Pricing Officer or any other authority;
 - (e) Records relating to the draft order;
 - (f) Evidence collected by, or caused to be collected by, it; and (g) Result of any enquiry made by, or caused to be made by it.
7. The Dispute Resolution Panel may, before issuing any directions referred to in sub-section (5),—
 - (a) Make such further enquiry, as it thinks fit; or
 - (b) Cause any further enquiry to be made by any income tax authority and report the result of the same to it.
8. The Dispute Resolution Panel may confirm, reduce or enhance the variations proposed in the draft order so, however, that it shall not set aside any proposed variation or issue any direction under sub-section (5) for further enquiry and passing of the assessment order.
9. If the members of the Dispute Resolution Panel differ in opinion on any point, the point shall be decided according to the opinion of the majority of the members.
10. Every direction issued by the Dispute Resolution Panel shall be binding on the Assessing Officer.
11. No direction under sub-section (5) shall be issued unless an opportunity of being heard is given to the assessee and the Assessing Officer on such directions which are prejudicial to the interest of the assessee or the interest of the revenue, respectively.
12. No direction under sub-section (5) shall be issued after nine months from the end of the month in which the draft order is forwarded to the eligible assessee.
13. Upon receipt of the directions issued under sub-section (5), the Assessing Officer shall, in conformity with the directions, complete, notwithstanding anything to the contrary contained in section 153, the assessment without providing any further opportunity of being heard to the assessee, within one month from the end of the month in which the direction is received.
14. The Board may make rules for the efficient functioning of the Dispute Resolution Panel and expeditious disposal of the objections filed, under subsection (2), by the eligible assessee.
15. For the purposes of this section,—
 - (a) “Dispute Resolution Panel” means a collegium comprising of 3 Commissioners of Income tax constituted by the Board for this purpose;
 - (b) “eligible assessee” means,—
 - (i) Any person in whose case the variation referred to in sub-section (1) arises as a consequence of the order of the Transfer Pricing Officer passed under sub-section (3) of section 92CA; and
 - (ii) any foreign company. Further, the following consequential amendments have been made—

- (i) Section 131(1) so as to provide that “Dispute Resolution Panel” shall have the same powers as are vested in a Court under the Code of Civil Procedure, 1908;
- (ii) Section 246(1)(a) has been amended so as to exclude the order of assessment passed under section 143(3) or order of re-assessment under section 147 in pursuance of directions of “Dispute Resolution Panel” as an appealable order.
- (iii) Section 253(1) has been amended to insert clause (d) so as to include an order of assessment passed under section 143(3) or order of re-assessment under section 147 in pursuance of directions of “Dispute Resolution Panel” as an appealable order.

An order passed under section 154 rectifying such order shall also be appealable to IT AT.

Income Escaping Assessment [Sec. 147]

If the Assessing Officer has reason to believe that any income chargeable to tax has escaped assessment for any assessment year, he may, following the prescribed process, assess or reassess such income and also any other income chargeable to tax which has escaped assessment and which comes to his notice subsequently in the course of the proceedings under this section, or recompute the loss or the depreciation allowance or any other allowance, as the case may be, for the assessment year concerned.

Where an assessment under section 143(3) or section 147 has been made for the relevant assessment year, no action shall be taken under this section after the expiry of four years from the end of the relevant assessment year, unless any income chargeable to tax has escaped assessment for such assessment year by reason of the failure on the part of the assessee to make a return under section 139 or section 142 or section 148 or to disclose fully and truly all material facts necessary for his assessment, for that assessment year.

Assessing Officer empowered to touch upon any other issue for which no reasons have been recorded notwithstanding that the reasons for such issue have not been included in the reasons recorded [Section 147] [W.r.e.f. assessment year 1989-90]

The existing provisions of section 147 provides, inter alia, that if the Assessing Officer has reason to believe that any income chargeable to tax has escaped assessment for any assessment year, he may assess or reassess such income after recording reasons for re-opening the assessment. Further, he may also assess or reassess such other income which has escaped assessment and which comes to his notice subsequently in the course of proceedings under this section.

Sonic Courts have held that the Assessing Officer has to restrict the reassessment proceedings only to issues in respect of which the reasons have been recorded for reopening the assessment. He is not empowered to touch upon any other issue for which no reasons have been recorded. The above interpretation is contrary to the legislative intent.

With a view to further clarifying the legislative intent, the Act has inserted Explanation 3 in section 147 to provide that the Assessing Officer may assess or reassess income in respect of any issue which comes to his notice subsequently in the course of proceedings under this section, notwithstanding that the reason for such issue has not been included in the reasons recorded under section 148(2).

Rationalisation of provisions of Tax Deduction and Collection at Source

Case Law :

A writ petition challenging reassessment, cannot be thrown out at the threshold on the ground that it is not maintainable - *Techspan India (P.) Ltd. v. ITO* 283 ITR 212 .

If the direction by the Commissioner is to reopen the assessment under section 147 by passing the statutory formalities, that would probably amount to dictating his subordinate to act in a particular way thereby taking away the discretion vested in the subordinate - *CIT v. Abdul Khader Ahamed* 156 Taxman 206.

Disclosure in wealth-tax proceedings will not suffice - *Arun Kumar Maheshwari v. ITO* 144 Taxman 651.

Sec. 148 : Issue of notice where income has escaped assessment.

- (1) Before making the assessment, reassessment or recomputation under section 147, the Assessing Officer shall serve on the assessee a notice requiring him to furnish within specified period, a return of his income.
- (2) The Assessing Officer shall, before issuing any notice under this section, record his reasons for doing so.



Legal Notes

- Notice under this section is to be mandatorily served by the Assessing Officer before initiating proceedings u/s 147. The notice is served on the assessee when it is received by him.
- Notice is to be issued within the time limits prescribed by section 149. Section 149(2) states that issue of such notice is subject to the provisions of section 151. Thus, approval for the issue of such notice is to be taken u/s 151 before its issue.
- Such notice can be issued by the Assessing Officer only after he records his reasons for doing so.
- The return to be furnished in response to such notice is treated as a return required to be furnished u/s 139 and the provisions of this Act, so far as may be, apply accordingly.
- Return in response to a notice under this section is to be furnished even if a return has been furnished earlier by the assessee under other provisions of the Act.
- Notice under this section can be issued even where an assessment u/s 143(3) has not been made but related intimations have been sent *Ranchi Club Ltd. v. CIT* 214 ITR 643

Case Law :

If reasons are supplied along with the notice under section 148(2), it shall obviate unnecessary harassment to the assessee as well as to the revenue by avoiding unnecessary litigation which will save courts also from being involved in unproductive litigation. Above all, it shall be in consonance with the principles of natural justice - *Mitlesh Kumar Tripathi v. CIT* 280 ITR 16

The notice prescribed by section 148 cannot be regarded as a mere procedural requirement. It is only if the said notice is served on the assessee that the ITO would be justified in taking proceedings against the assessee. If no notice is issued or if the notice issued is shown to be invalid, then the proceedings taken by the ITO would be illegal and void - *Y. Narayana Chetty v. ITO* [1959] 35 ITR 388; *CIT v. Thayaballi Mulla Jeevaji Kapasi* 66 ITR 147; *CIT v. Kurban Hussain Ibrahimji Mithiborwala* 82 ITR 821

Where the AAC set aside the reassessment on the only ground that the assessee was not afforded opportunity to put forward his case, but did not hold that the notice issued under section 148 was invalid, there would be no need for the ITO to issue a fresh notice to the assessee - *CIT v. T.S.P.L.P. Chidambaram Chettiar* 80 ITR 467.

Notice cannot be issued unless the return which has already been filed has been disposed of - *CIT v. M.K.K.R. Muthukaruppan Chettiar* 78 ITR 69; *Bhagwan Das Sita Ram (HUF) v. CIT* 146 ITR 563.

Sec. 149 : Time limit for notice.

(1) No notice under section 148 shall be issued for the relevant assessment year —

- if four years have elapsed from the end of the relevant assessment year, unless the case falls under clause (b);
- if four years, but not more than six years, have elapsed from the end of the relevant assessment year unless the income chargeable to tax which has escaped assessment amounts to or is likely to amount to one lakh rupees or more for that year.
 - Time-limit applies for 'Issue' and not for service - *R.K. Upadhyaya v. Shanabhai P Patel* [1987] 166 ITR 163 (SC).
 - Amended law will apply only if limitation has not already expired - *Chandiram v. ITO* [1996] 87 Taxman 418 (Raj.).

The word 'issued' in section 149 should be given its natural meaning and not the strained wider meaning of 'served'. Consequently, where the notice was issued within time but was served on the assessee after the expiry of the time-limit, it could not be held to be invalid - *R.K. Upadhyaya v. Shanabhai P. Patel* 166 ITR 163 (SC); *CIT v. Sheo Kumari Debi* 157 ITR 13 and *Jai Hanuman Trading Co. (P.) Ltd. v. CIT* 110 ITR 36.

Provision for cases where assessment is in pursuance of an order on appeal, etc. [Sec. 150]

- (1) Notwithstanding anything contained in section 149, the notice under section 148 may be issued at any time for the purpose of making an assessment or reassessment or recomputation in consequence of or to give an effect to any finding or direction contained in an order passed by any authority in any proceeding under this Act by way of appeal, reference or revision or by a Court in any proceeding under any other law.
- (2) The provisions of sub-section (1) shall not apply in any case where any such assessment, reassessment or recomputation as is referred to in that sub-section relates to an assessment year in respect of which an assessment, reassessment or recomputation could not have been made at the time the order which was the subject-matter of the appeal, reference or revision, as the case may be, was made by reason of any other provision limiting the time within which any action for assessment, reassessment or recomputation may be taken.
 - This section prescribes the time limit for issuance of notice u/s 148 in a special case. This section overrides the provisions of section 149. Section 149 vide sub-section (2) provides that issue of notice u/s 148 is subject to the provisions of section 151. Thus, approval u/s 151 for issue of notice u/s 148(1) is not required in a case covered by section 150 {Sukhdayal Pahwa v. CIT [1983] 140 ITR 206 (MP)}.
 - Notwithstanding the time limits prescribed by section 149, notice u/s 148 can be issued at any time for making assessment, etc., to give effect to any finding or direction referred to in sub-section (1). The order referred to therein may be an order u/s 250, 254, 260, 262, 263 or 264.
 - The power conferred by sub-section (1) to the revenue for making assessment, etc., is withdrawn in a special case covered by sub-section (2). This covers a case where the order for an assessment year is made such order being the subject matter of an appeal, reference or revision, the finding or direction of which results in an assessment, etc., referred to in sub-section (1). However, at the time such order is made, the assessment etc, in respect of that a.y. is itself time barred by virtue of any other provision of this Act. Sub-section (2) applies to such cases.
 - Also see Explanations 2 and 3 to section 153.

Sanction for issue of notice [Sec. 151]

- (1) In a case where an assessment under sub-section (3) of section 143 or section 147 has been made for the relevant assessment year, no notice shall be issued under section 148 by an Assessing Officer, who is below the rank of Assistant Commissioner or Deputy Commissioner, unless the Joint Commissioner is satisfied on the reasons recorded by such Assessing Officer that it is a fit case for the issue of such notice:

Provided that, after the expiry of four years from the end of the relevant assessment year, no such notice shall be issued unless the Chief Commissioner or Commissioner is satisfied, on the reasons recorded by the Assessing Officer aforesaid, that it is a fit case for the issue of such notice.

- (2) In a case other than a case falling under sub-section (1), no notice shall be issued under section 148 by an Assessing Officer, who is below the rank of Joint Commissioner, after the expiry of four years from the end of the relevant assessment year, unless the Joint Commissioner is satisfied, on the reasons recorded by such Assessing Officer, that it is a fit case for the issue of such notice.
 - Reasons need not be communicated to assessee
 - Commissioner must not accord sanction mechanically
 - Assent must be commissioners own hand
 - Commissioner must give fair hearing to assessee
 - Whether a mere yes or no endorsement will suffice.

**Case Law:**

There is no requirement in any of the provisions of the Act or any section laying down as a condition for the initiation of the proceedings that the reasons which induced the Commissioner to accord sanction to proceed under section 147 must also be communicated to the assessee *S. Narayanappa v. CIT* 63 ITR 219 .

Sec. 152 : Other provisions.

- (1) In an assessment, reassessment or recomputation made under section 147, the tax shall be chargeable at the rate or rates at which it would have been charged had the income not escaped assessment.
- (2) Where an assessment is reopened under section 147, the assessee may, if he has not impugned any part of the original assessment order for that year either under sections 246 to 248 or under section 264, claim that the proceedings under section 147 shall be dropped on his showing that he had been assessed on an amount or to a sum not lower than what he would be rightly liable for even if the income alleged to have escaped assessment had been taken into account, or the assessment or computation had been properly made :

Provided that in so doing he shall not be entitled to reopen matters concluded by an order under section 154, 155, 260, 262 or 263.

Section 153: Time limit for completion of assessment and reassessment.

Regular assessment U/s 143 or 144 must be made within twenty-one months of the relevant assessment year or one year end of the Financial Year in which the return was filed whichever is later.

Assessment in case of search or requisition [Section 153A]

Notwithstanding anything contained in section 139, section 147, section 148, section 149, section 151 and section 153, in the case of a person where a search is initiated under section 132 or books of account, other documents or any assets are requisitioned under section 132A after the 31st day of May, 2003, the Assessing Officer shall—

- (a) issue notice to such person requiring him to furnish within such period, as may be specified in the notice, the return of income in respect of each assessment year falling within six assessment years referred to in clause (b), in the prescribed form and verified in the prescribed manner and setting forth such other particulars as may be prescribed and the provisions of this Act shall, so far as may be, apply accordingly as if such return were a return required to be furnished under section 139;
- (b) assess or reassess the total income of six assessment years immediately preceding the assessment year relevant to the previous year in which such search is conducted or requisition is made :

The Assessing Officer shall assess or reassess the total income in respect of each assessment year falling within such six assessment years:

It is provided that assessment or reassessment, if any, relating to any assessment year falling within the period of six assessment years referred to in this section pending on the date of initiation of the search under section 132 or making of requisition under section 132A, as the case may be, shall abate.

Except as otherwise provided in this section, section 153B and section 153C, all other provisions of this Act shall apply to the assessment made under this section;

In an assessment or reassessment made in respect of an assessment year under this section, the tax shall be chargeable at the rate or rates as applicable to such assessment year.

Prior approval necessary for assessment in cases of search or requisition [Sec. 153D]

No order of assessment or reassessment shall be passed by an Assessing Officer below the rank of Joint Commissioner in respect of each assessment year referred to in clause (b) of section 153A or the assessment year referred to in clause (b) of sub-section (1) of section 153B, except with the prior approval of the Joint Commissioner."

QUESTIONS & ANSWERS ON ASSESSMENT PROCEDURE

Question 1: What is a protective assessment under Income-tax law? What is the procedure followed for the recovery of tax in such cases?

Answer: A protective assessment is made in a case where there are doubts relating to the true ownership of the income. If there is an uncertainty about the taxing of an income in the hands of Mr. A or Mr. B, then at the discretion of the Assessing Officer, the same may be added in the hands of one of them on protective basis. This is to ensure that on finality, the addition may not be denied on the ground of limitation of time. Once finality regarding the identity of the tax payer to be taxed is established, the extra assessment is cancelled. But the Department cannot recover the tax from both the assesseees in respect of the same income. Penalty cannot be imposed on the strength of a protective assessment.

Question 2: Joseph engaged in profession filed his return of income for assessment year 2011-12 on 15th November, 2011. He disclosed an income of ₹4,00,000 in the return. In February, 2012 he discovered that he did not claim certain expenses and filed a revised return on 3rd February, 2012 showing an income of ₹1,80,000 and claiming those expenses. Is the revised return filed by Joseph acceptable?

Answer: Joseph is engaged in profession. The due date for filing income tax return for assessment year 2011-12 as per section 139(1) of the Income-tax Act is 30th September, 2011 if his accounts are required to be audited under any law. The due date is 31st July, 2011 if the accounts are not required to be audited under any law.

The return was filed beyond the due date prescribed in section 139(1). The return so filed is covered by section 139(4) and the time limit is one year from the end of the relevant assessment year. The Apex court in *Kumar Jagadish Chandra Sinha v. CIT 220 ITR 67 (SC)* has held that a return filed under section 139(4) is not eligible for revision and hence a revised return cannot be filed.

Hence, the return filed by Joseph is not valid as the original return was not filed before the due date mentioned in section 139(1).

Question 3: An assessee filed a return of income on 31.8.2011 in respect of Assessment year 2011-12 disclosing an income of ₹5 lakhs from business. It was not accompanied by proof of payment of tax due on self-assessment. Discuss the validity of such a return.

Answer: As per Explanation to sub-section (9) of section 139 a return is regarded as defective unless it is accompanied by proof of tax deducted at source, advance tax and tax on self-assessment, if any, claimed to have been paid. Therefore, the return is prima facie defective. It is not invalid at that stage. On receipt of the return, the Assessing Officer has to intimate the defect to the assessee and give him an opportunity to rectify the defect within a period of 15 days from the date of such intimation or within such further period which, on application by the assessee, he may, in his discretion allow. If the defect is not rectified within the said period, the return will be treated as an invalid return and the provisions of the Income-tax Act shall apply, as if the assessee has failed to furnish the return. Also, it may be noted that section 140A(3) says that if an assessee fails to pay tax or interest on self assessment he shall be deemed to be an assessee in default in respect of the tax or interest or both remaining unpaid and all the provisions of the Act shall apply accordingly.

Question 4: If an assessment is remanded back to Assessing Officer, can he introduce new sources of income for assessment?

Answer: Where the assessment is set aside by the Tribunal and the matter remanded to the Assessing Officer, it is not open to him to introduce into the assessment new sources of income so as to enhance the assessment. Any power to enhance is confined to the old sources of income which were the subject matter of appeal [*Kartar Singh vs. CIT (1978) 111 ITR 184 (P & H)*].

Question 5: Can Department make fresh computation, once the assessment is made final?

Answer: It is now a well settled principle that an assessment once made is final and that it is not open to the department to go on making fresh computation and issuing fresh notices of demand to the end of all time. [*ITO vs. Habibullah (S.K.) (1962) 44 ITR 809 (SC)*]



Question 6: Can an Assessing Officer make an assessment for a year other than the assessment year for which the return is filed?

Answer: It is not open to the Assessing Officer to make assessment in respect of a year other than the Assessment Year for which the return is filed. Thus, in respect of a return filed for assessment year 2010-11, assessment cannot be made for the assessment year 2011-12. [CIT vs. Amaimugan Transports Pvt.Ltd.(1995) 215 ITR 553 (Mad.)]

Question 7: Can an Assessing Officer assess the income below the returned income or assess the loss higher than the returned loss?

Answer: The Assessing Officer cannot assess income under section 144 for an assessment below the returned income or cannot assess the loss higher than the returned loss.

Question 8: Can incomplete, unsigned or unverified return lead to best judgement assessment?

Answer: Incomplete, unsigned or unverified return may lead to best judgement assessment. A best judgement assessment can be made when the return is filed woefully incomplete or not signed and verified. [Behari Lal Chatterji vs.CIT (1934) 2 ITR 377 (All.)]

Question 9: Can assessee follow different method of accounting for different businesses?

Answer: If an assessee is carrying on more than one business, he can follow cash system of accounting for one business and mercantile system (accrual system) of accounting for other business. Similarly, if he had more than one sources of income under the head income from other sources, he can follow accrual system for one source of income under the head income from other sources, he can follow accrual system for one and cash system for other sources of income.

Question 10: What can Assessing Officer do when the assessment is not set aside for fresh assessment but annulled?

Answer: Where an assessment is not set aside for fresh assessment but annulled, no extended limitation is available. However, if the original time limit is available, the Assessing Officer may proceed from the stage at which illegality which resulted into the annulment of the assessment supervened and make the assessment afresh. [CIT vs.Mrs.Ratanbai N.K. Dubhash (1998) 230 ITR 495(Bom.)]

STUDY NOTE - 17

ASSESSMENT OF VARIOUS ENTITIES

This Study Note includes

- Provisions relating to Assessment of Various Entities

ASSESSMENT OF VARIOUS ENTITIES

17.1 ASSESSMENT OF INDIVIDUALS

Tax incidence on Individuals

While computing taxable Income of an Individual following points should be considered.

Nature of Income	Tax Treatment
Income earned by the taxpayer	Except the following all other incomes shall be included (a) income exempt under sections 10 to 13A (b) incomes to be included in income of others by virtue of section 60 to 64.
Share of Profit from Hindu undivided family	It is exempt under section 10(2)
Share of Profit from a firm assessed as firm	It is exempt under section 10(2A)
Salary and Interest from the aforesaid firm	These are taxable as business Income
Share of profit from an association of persons/body of Individuals	If the association/body is taxable at the maximum marginal rate (or at higher rate), then share of profit is not taxable in hands of recipient.
Income earned by others and included in the income of the taxpayer by virtue of section 60 to 64	Such income shall be included in the income of the taxpayer.

Special Provisions for persons governed by Portuguese Civil law (Section 5A)

This Section is applicable for the appropriation of income between spouses governed by the Portuguese Civil Code which is in force in the state of Goa and Union territories of Dadra and Nagar Haveli and Daman and Diu. By virtue of this section, income from all other sources, except from salary, should be apportioned equally between husband and wife. The income so apportioned will be included separately in the total income of the husband and of the wife and the remaining provisions of act shall apply accordingly. Salary Income is, however, taxable in the hands of the spouse who has actually earned it.

Even the income from profession will be apportioned equally between the husband and the wife-

CIT v Datta V Gaitonde [2002] 241 ITR 241/108/ taxman 533(Bom).

Taxable income- How computed



Taxable income shall be computed as follows :

- Step 1- Income under the different heads of income -First find out income under the five heads of income
- Step 2- Adjustment of losses of the current year and earlier years- Losses should be setoff according to the provisions of sections 70 to 78. The income after adjustment of losses is the gross total income.
- Step 3- Deduction from gross total income- Deductions specified under Chapter VI A should be considered while calculating the gross total income.
- Step 4- Rounding off- The balance should be rounded off to the nearest ₹ 10. it is called as net income or taxable income or total income.

Tax liability :

Normal Rates of Income Tax

In the case of every Individual or Hindu undivided family or AOP/BOI (other than a co-operative society) whether incorporated or not, or every artificial judicial person

Upto ₹ 1,80,000	Nil
₹ 1,80,010 to ₹ 5,00,000	10%
₹ 5,00,010 to ₹ 8,00,000	20%
Above ₹ 8,00,000	30%

II. In the case of every **individual**, being a **woman resident in India**, and **below the age of sixty years** at any time during the previous year.

Upto ₹ 1,90,000	Nil
₹ 1,90,010 to ₹ 5,00,000	10%
₹ 5,00,010 to ₹ 8,00,000	20%
Above ₹ 8,00,000	30%

III. In the case of every **individual**, being a **resident in India**, who is of the **age of 60 years or more** at any time during the previous year. [*Senior citizen*]

Upto ₹ 2,50,000	Nil
₹ 2,50,010 to ₹ 5,00,000	10%
₹ 5,00,010 to ₹ 8,00,000	20%
Above ₹ 8,00,000	30%

IV. In the case of every **individual**, being a **resident in India**, who is of the **age of 80 years or more** at any time during the previous year. [**Very senior citizen**]

Upto ₹ 5,00,000	Nil
₹ 5,00,010 to ₹ 8,00,000	20%
Above ₹ 8,00,000	30%

Note : No surcharge is payable by the above assessees.

'Education Cess' @ 2%, and 'Secondary and Higher Education Cess (SHEC)' @ 1% on income tax shall be chargeable.

Special Provisions relating to non-residents [Section 115C to 115I]

The benefit of Special provisions can be claimed by non-resident Indians. The following are non-resident Indians for the purpose:

- a. citizen of India who is a non-resident ;
- b. a person of Indian origin who is a non-resident.

A person shall be deemed to be of Indian origin if he or either of his parents or any of his grandparents, was born in an undivided India.

The Provisions of Section 115C to 115I are applicable only in respect of the following incomes derived a non resident Indian:

- a. investment income derived from a “foreign exchange assets”; and
- b. long term capital gains on sale or transfer of “foreign exchange assets”.

Foreign Exchange Asset- It means those “specified asset” which the assessee has acquired or purchased with, or subscribed to in, convertible foreign exchange;

The following are the “specified assets”:

- a. shares in an Indian Company (public or private)
- b. debentures issued by an Indian Company which is not a private company ;
- c. deposits with an Indian Company which is not a private Company, it may be even deposit with SBI or any other banking company;
- d. any security of the Central Government ; and
- e. such other asset as the Central Government may specify in this behalf by notification in the Official Gazette.

Investment Income

In computing the Investment income of a non-resident Indian, no deduction in respect of any expenditure or allowance shall be allowed under any provision of the Act. Moreover, no deduction under Sections 80C to 80U shall be allowed in respect of investment income of non –resident Indians.

Long term Capital gain

Long term Capital gain on sale or transfer of foreign exchange assets shall be calculated subject to:

1. The benefit of Indexation is not available for the sale or transfer of foreign exchange assets.
2. The non-resident Indian can claim exemption under section 115F by investing sale consideration in another asset.
3. No deduction is permissible under section 80C to 80U in respect of long term capital gain.

Tax treatment on Investment and long term capital Gain:

Non resident Indians are chargeable to tax on investment and long term capital gain at the rate of 20 percent and 10 percent respectively.(plus surcharge and education cess)

Return of Income not to be filled in certain cases:

Where a non-resident Indian has income only from a foreign exchange asset or income by way of long term capital gains arising on transfer of a foreign exchange asset, or both, and tax deductible at source from such income has been deducted, he is not required to file the return of income under section 139(1).

The income from foreign exchange assets and long term capital gains arising on transfer of such assets would be treated as separate block and charged to tax at a flat rate as explained above.

If the non-resident Indian has other Income in India, such other income is treated as an altogether separate block and charged to tax in accordance with other provisions of the Act.

Benefit available even after the assessee becomes resident – These provisions are as follows:

1. A non-resident Indian in any previous year, becomes assessable as resident in India in any subsequent year.
2. He may furnish to the Assessing Officer a declaration in writing(along with his return of income under section 139 for the assessment year for which he is so assessable)to the effect that the special provisions shall continue to apply to him in relation to the investment income derived from any foreign exchange asset.



3. The foreign exchange assets for this purpose are debentures and deposit with an Indian public limited company and Central Government securities.

The special provisions shall continue to apply for that assessment year and for every subsequent assessment year till the transfer or conversion (otherwise than by transfer) into money of such assets.

Special Provisions not to apply if the assessee so chooses (section 115-I)

A non Resident Indian may opt that the special provisions should not apply to him by making a declaration to that effect in his return of income for the relevant assessment year. In such case the whole of his Income (including income from foreign exchange assets and long term capital gains arising on transfer of a foreign exchange asset) is chargeable to tax under the general provisions of the Act.

17.2 ASSESSMENT OF HINDU UNDIVIDED FAMILY

U/s. 4 of the Income Tax Act, 1961, Income-tax is payable by 'every person'. 'Person' includes a 'Hindu Undivided Family' as defined in sec. 2(31). The definition of 'Hindu Undivided Family' is not found in the Income-tax Act. Therefore the expression 'Hindu Undivided Family' must be construed in the sense in which it is understood under the 'Hindu Law' [Surjit Lal Chhabda vs. CIT 101 ITR 776(SC)].

According to Hindu Law, 'Hindu Undivided Family' is a family which consists of all persons lineally descended from a common ancestor and includes their wives and unmarried daughters. A 'Hindu Undivided Family' is neither the creation of law nor of a contract but arises from status.

A Hindu coparcenary includes those persons who acquire by birth an interest in joint family property. Only a male member of a family can be a coparcener while the membership of a HUF consists of both males and females. All the coparceners of the family constitute what is called a 'Coparcenery'. All the coparceners are members of a HUF but all members of a HUF are not coparceners. A coparcener of a joint family, who acquires by birth an interest in the joint property of the family, whether inherited or otherwise acquired by the family, may have a right to enforce partition whereas the members of the family who are not coparceners have no right to enforce partition. When a partition takes place, member (mother or widow) of the joint family may get a share equal to the sons and also it is necessary to provide for maintenance and marriage of the unmarried daughter out of family property.

There are two schools of Hindu Law- 1) Mitakshara and 2) Dayabhaga. Under the Mitakshara school, each son acquires by birth an equal interest with his father in the ancestral property. Under the Dayabhaga School which prevails in West Bengal and Assam, a son does not acquire by birth in ancestral property. He acquires interest only on the death of his father. Father enjoys an absolute right to dispose of the property of the family according to his desire. After the death of father, his son does not, by operation of law, become members of the joint family. The sons remain as co-owners with definite shares in the properties left by father unless they decide to live as a joint family.

Case Laws:

(i) A single person, male or female, cannot constitute a Hindu Undivided Family. An individual, who has obtained a share on partition of a joint family, has potentialities of creating a joint family; but until he marries, he alone cannot be considered as a joint family. C. Krishna Prasad vs. CIT 97 ITR 493.

(ii) A joint family may consist of a single male member with his wife and daughter(s) and it is not necessary that there should be two male members to constitute a joint family [Gowli Buddanna vs. CIT 60 ITR 193].

Jain & Sikh families are not governed by Hindu Law. However, for the purpose of Income tax Act, such families are treated as 'Hindu Undivided Families'.

The income of a joint Hindu family may be assessed in the status of HUF if the following conditions are satisfied:-

- (i) there should be a coparcenership
- (ii) there should be a joint family property which consists of ancestral property, property acquired with the aid of ancestral property and property transferred by its members. It may be pointed out that once a joint family income is assessed as that of Hindu Undivided Family, it will continue to be assessed as such in future years till partition is claimed by its coparceners.

Under the Hindu Law, ancestral property is the property which a person inherits from any of this three immediate male ancestors, i.e. his father, grand father and great grand father. Income of ancestral property is taxable as income of HUF in the following cases:

- (i) family of husband and wife without any children;
- (ii) family of two widows of deceased brothers;
- (iii) family of two or more brothers;
- (iv) family of uncle and nephew;
- (v) family of mother, son and son's wife;
- (vi) family of a person and his late brother's wife;
- (vii) family of widow mother and her sons.

While computing income of a Hindu Undivided Family one should give due consideration of the following :

- (i) where a member of HUF converts his self acquired property into joint family, income from such property shall not be treated as income of HUF u/s. 64(2). It shall continued to be taxed in the hands of the transferor who is the member of the HUF.
- (ii) Income from an impartible estate is taxable in the hands of the holder of the estate and not in the hands of HUF.
- (iii) income from Stridhan of a woman is not taxable in the hands of HUF.
- (iv) personal income of members cannot be treated as income of HUF.
- (v) where the funds of HUF are invested in a company or a firm, fees or remuneration received by the member as a director or a partner in the company or a firm may be treated as income of HUF in case the fees and remuneration is earned essentially as a result of investment funds
- (vi) where remuneration is paid by HUF to Karta or any other member for services rendered by him in conducting family's business, the remuneration is deductible provided the remuneration is paid :
 - (i) under a valid bonafide agreement;
 - (ii) in the interest of, and expedient for the business family, and
 - (iii) genuine and not unreasonable.

Case law:

- (i) remuneration and commission received by the Karta of HUF on account of his personal qualifications and exertions and not on account of investments of the family funds in the company cannot be treated as income of HUF. Subbiah Pillai (K.S.) vs. CIT103 Taxman 400/237 ITR 11

PARTITION OF HUF

'Partition' may be a (i) total or complete partition (ii) partial partition.

Where all the properties of the family are divided amongst all the members of the family, and the family ceases to exist as an undivided family, it is known as total or complete partition.

On the other hand, where one or more coparceners of the HUF may separate from others and the remaining coparceners may continue to be joint or some of the properties are divided and the balance remain joint it is known as partial partition.

W.e.f. 31st December, 1978 partial partition are not recognised for tax purposes and as such the joint family shall continue to be liable to be assessed as if no such partial partition had taken place. Each member of such family, immediately before such partial partition and the family shall be jointly and severally liable for any sum payable under the Act. [Sec. 171(9)]



17.3 ASSESSMENT OF FIRMS

From the Assessment Year 1993-94 partnership firm has been classified for the purpose of computation of income and its assessment as under:

- (a) partnership firm assessed as such (PFAS)
- (b) partnership firm assessed as an association of person.

Provisions relating to assessment of firms and partners are analyzed as under :

Specific provisions to firm assessed as an AOP

Particulars	Sections
Disallowance of salary and interest to partner	40(ba)
Method of computing partner's share in the income of PFAOP	67A
Rate of tax in respect of income of AOP/BOI	167B
Taxability of partner's share of income	86, 110

Assessment of firms and conditions to be fulfilled to avail the status of PFAS [Sec. 184]

Where a firm wants to avail the status of PFAS, it has to satisfy the following conditions:-

- (i) The firm shall be evidenced by an instrument and the individual shares of the partner shall be specified therein. [Sec. 184(1)]
- (ii) A certified copy of the instrument of partnership shall accompany the return of income of the previous year relevant to the assessment year 1993-94 or sub sequent year in respect of which assessment of the firm is first sought. [Sec.184(2)]
- (iii) Wherever during a previous year a change takes place in the constitution of the firm or in the sharing ratio of partners, a certified copy of the revised instru ment of partnership be submitted along with the return of income of the concerned year of assessment. [Sec. 184(4)]
- (iv) There should not be any failure on the part of the firm as is specified in Sec. 144 [Sec. 184(5)]

It may be mentioned that once a firm is assessed as PFAS after fulfillment of the above conditions, it will be assessed as PFAS, for every subsequent year provided there is no change in either firm's constitution or partner's profit sharing ratio. However, there should not be any failure mentioned in sec. 144. [Sec. 184(3)]

A partnership deed shall be certified in writing by all the major partners. Where, however, the firm is dissolved and the return is filed after its dissolution, then the copy of deed may be certified by all the major partners in the firm immediately before is dissolution. Where a partner is dead, then it will have to be certified by his legal representative. [Sec. 184(2) Expl.]

Computation of Income

The following provisions should be given due consideration while computing income of a firm-

- (i) Provision relating to deductibility of remuneration paid to partners by firm.
- (ii) Provision relating to deductibility of interest paid to partners by firm.

17.4 ASSESSMENT OF ASSOCIATION OF PERSONS / BODY OF INDIVIDUALS

Association of Persons :

Where two or more persons voluntarily joint together in a common purpose or action with the object of producing income, Profits and gains they are said to have formed an Association of Persons.

Body of Individuals:

It is a conglomerate of individuals who happen to have come together to carry on sum activity with a view to earn income i.e. co-heirs inheriting shares or securities.

Distinction between AOP & BOI :

- (i) AOP may consist of non-individuals but BOI has to consist of individuals only
- (ii) An AOP is a voluntary combination of persons in a joint enterprise or common action to produce income whereas in case of BOI will only consist of two or more persons, may or may not have any common object.
- (iii) A BOI may become an AOP, but not *vice versa*.

Share of members of AOP/BOI shall be deemed to be indeterminate or unknown, if such shares (in relation to the whole or any part of the income) are indeterminate or unknown on the date of formation of such AOP/BOI or any time thereafter.

Any payment of interest, salary, bonus, commission or remuneration by the AOP/BOI to a member is not allowable as deduction. Where interest is paid by AOP/BOI to a member who has also paid interest to the AOP/BOI, the amount of interest to be disallowed will be limited to the net amount of interest paid by the AOP/BOI. [Sec. 40(ba)]

Tax Rates :

	Where shares of members are determinate and known	Where shares of members are indeterminate or unknown
1. None of the members having taxable income	At the rates applicable to individual	At the maximum marginal rate.
2. Any member having income.	At the maximum marginal rate	At the maximum taxable marginal rate.

Maximum marginal rate means the rate of tax (including surcharge, if any) applicable to the highest slab of income in case of individuals. [Sec.2(29C)]

Ascertainment of member's share in AOP/BOI where shares are determinate and its taxability [Sec. 67A, 86 & 110]

(i) Ascertainment of share in AOP/BOI [Sec. 67A]	₹
Total income of the AOP/BOI	***
Less: Interest, salary, commission or other remuneration paid to any member	***
Balance apportionable to the members in proportion to their shares	***
Share of income allotted to a member	***
Add: Salary, interest, commission or other remuneration received by the member of the AOP or BOI	***
Total share	***
Less: Interest paid on capital borrowed for the purpose of investment in the AOP/BOI	***
Net assessable share income	***

(ii) Tax treatment of share income of members [Sec. 86 and Sec. 110]

In computing total income of an assessee, there shall be included share income of a member of an AOP or BOI subject to sec. 86 and 110 of the I.T. Act.



Taxation of AOP/BOI [Sec 167B]	Tax treatment of share income in the hands of members of AOP/BOI [Sec. 86 & 110]
1. AOP or BOI is taxed at maximum marginal rate or at a higher rate.	Share income of the member is not taxable.
2. AOP or BOI is taxed at normal rates applicable	Share income computed u/s. 67A is included into an Individual. the total income of the member but rebate u/s. 110 at the average of tax in respect of such share income has to be allowed.
3. AOP or BOI is not taxed at all.	Share income will be included in the total income of the member and taxed at the rates applicable to him.

“Average rate of Income-tax” is defined u/s. 2(10) to mean the rate arrived at by dividing the amount of Income-tax calculated on the total income, by such total income.

17.5 ASSESSMENT OF COMPANIES

In computing tax incidence companies are classified as follows :

- (i) Domestic Company
- (ii) Foreign Company

‘Company’ means —

- (i) any Indian company; or
- (ii) body corporate incorporated outside India under the laws of a foreign country; or
- (iii) any institution, association or a body which is assessed or was assessable/assessed as a company for any assessment year commencing on or before 1.4.1970; or
- (iv) any institution, association or body whether incorporated or not and whether Indian or non-Indian which is declared by general or special order of the Central Board of Direct Taxes to be a company. [Sec. 2(17)]

‘Domestic Company’ means —

- (i) an Indian company; or
- (ii) any other company which, in respect of its income liable to tax under the Act, has made the following prescribed arrangements for the declaration and pay ment of dividends within India in accordance with Sec. 194 read with Rule 27 of the Rules:
 - (a) The share register of the company for all shareholders should be regularly maintained at its principal place of business in India, in respect of any assessment year, from 1st April of the relevant assessment year.
 - (b) The general meeting for passing of accounts of the relevant previous year and for declaring dividends in respect thereof should be held only at a place within India.
 - (c) The dividends declared, if any, should be payable only within India to all shareholders. [Sec. 2(22A)]

‘Foreign Company’ means company which is not a domestic company. [Sec. 2(23A)]

‘Indian Company’ means a company formed and registered under the Companies Act, 1956. Besides, it includes the following:-

- (a) a company formed and registered under any law relating to companies formerly in force in any part of India;
- (b) a corporation established by or under a Central, State or Provincial Act;

- (c) any institution, association or body which is declared by the Board to be a company u/s. 2(17).
- (d) a company formed and registered under any law in force in the State of Jammu and Kashmir;
- (e) a company formed and registered under any law for the time being in force in the Union territories of Dadra and Nagar Haveli, Daman and Diu, Pondicherry and State of Goa.

In the aforesaid cases, a company, corporation, institution, association or body will be treated as an Indian company only if its registered or principal office is in India. [Sec. 2(26)]

“Company’ in which the public are substantially interested” –

a company is said to be a company in which the public are substantially interested, if-

- (a) a company owned by Government or Reserve Bank of India or in which not less than 40% shares are held singly or taken together by the Government or the Reserve Bank or a corporation owned by the Reserve Bank; or
- (b) it is a company registered u/s. 25 of the Companies Act, 1956, i.e., companies incorporated for promotion of Commerce, Arts, Science, Religion, Charity and prohibiting the payment of any dividends to its members; or
- (c) it is a company having no share capital and it is declared by the CBDT to be a company in which the public are substantially interested; or
- (d) it is a company which carries on, as its principal business, the business of acceptance of deposits from its members and which is declared by the Central Government u/s. 620A of the Companies Act to be a Nidhi or Mutual Benefit Society; or
- (e) it is a company which is not a private company and its equity shares are, as on the last day of previous year, listed in a recognised stock exchange in India; or
- (f) it is a company which is not a private company and its shares carrying not less than 50% of the voting power (40% in the case of Indian companies whose business consists mainly in the construction of ships or in the manufacture or processing of goods or in mining or in the generation or distribution of electricity or any other form of power) have been allotted unconditionally to or acquired unconditionally to, or acquired unconditionally by, and were through out the relevant previous year beneficially held by-
 - (i) the Government; or
 - (ii) a statutory corporation; or
 - (iii) a company in which the public are substantially interested or any wholly owned subsidiary of such company.
- (g) it is a company, wherein equity shares carrying not less than 50% of the voting power have been unconditionally allotted to or acquired by and were through out the relevant previous year beneficially held by, one or more cooperative societies. [Sec. 2(18)]

Minimum alternative tax on certain companies

A company is liable to pay tax on the total income computed in accordance with the provisions of the Income Tax Act, but the profit and loss account is prepared as per provisions of the Companies Act. There were large number of companies who had book profits as per profit and loss account but the total income as per provision of the Income-tax Act was either nil or negative or insignificant and as a result such companies were not paying any income-tax through sometimes, such companies were paying dividends to shareholder. These companies are popularly known as “Zero tax companies”.

In order to bring these companies under the Income-tax Act, the following sections were included time to time from assessment year 1997-98.

“Average rate of Income-tax” is defined u/s. 2(10) to mean the rate arrived at by dividing the amount of Income-tax calculated on the total income, by such total income.

**AMALGAMATION [Sec. 2(1B)]**

Amalgamation in relation to companies means the merger of one or more companies with another company, or merger of two or more companies to form a new company. The company so merged goes out of existence is “amalgamating company.” The company into which the amalgamating company merges, or the new company that is formed to effect amalgamation, is “amalgamated company” in such a manner that :-

- (a) All property of amalgamating company, immediately before amalgamation, should become the property of amalgamated company,
- (b) All liabilities of amalgamating company, immediately before amalgamation, should become the liabilities of amalgamated company,
- (c) Shareholders holding 75% in value of the shares in amalgamating company should become shareholders of the amalgamated company. However, if the amalgamated company or its subsidiary/nominee already holds some shares in the amalgamating company, value of such shares is excluded for calculating 75% of the value of shares of the amalgamating company.

A merger of companies will not be treated as amalgamation in case of sale or liquidation of company.

The effective date in a scheme of amalgamation is the date of transfer specified in the scheme and not the date of high court's order approving the scheme. So long as the court does not modify the date specified in the scheme, amalgamation takes effect on date of transfer specified in the scheme. The income of the amalgamating company from such date of transfer shall be assessed as income of the amalgamated company and shall be assessed accordingly. [Marshall Sons and Co. (India) Ltd. v. ITO (SC), 223 ITR 809]

Certain concessions are provided under various provisions of the Income-tax Act in respect of amalgamation which are as under:

(a) To amalgamating company

- (i) Sec. 47 (vi): In a scheme of amalgamation capital gains tax is not attracted in case of transfer of capital asset by the amalgamating company to the amalgamated company.
- (ii) Sec. 47(via): Tax concession to foreign amalgamating company.

(b) To shareholders of an amalgamating company

Sec.47(vii) : Transfer by a shareholder in a scheme of amalgamation of a capital asset being a share or shares held by him in amalgamating company.

(c) To amalgamated company

The following benefits in the hands of amalgamating company are available to the amalgamated company:

- Sec. 35(5) : Expenditure on scientific research
- Sec. 35A(6) : Expenditure on acquisition of patent right or copy right
- Sec. 35AB(3) : Expenditure on know how
- Sec. 35ABB(6) : Expenditure for obtaining license to operate telecommunication services
- Sec. 35D(5) : Amortisation of preliminary expenses
- Sec. 36E(7) : Deduction for expenditure on prospecting etc. for certain minerals
- Sec. 36(ix) : Expenditure incurred for the purpose of promoting family planning.
- Sec. 72A : Carry forward and set off of accumulated and unabsorbed depreciation

Further, the amalgamated company is entitled for :

Sec. 35DD : Amortisation of expenditure in case of amalgamation or demerger

DEMERGER SEC. 2(19AA)

“Demerger” in relation to companies, means the transfer, pursuant to a scheme of arrangement under sections 391 to 394 of the Companies Act, 1956, by a demerged company of its one or more undertakings to any resulting company in such a manner that —

- (i) all the property of the undertaking, being transferred by the demerged company, immediately before the demerger, becomes the property of the resulting company by virtue of the demerger;
- (ii) all the liabilities relating to the undertaking being transferred by the demerged company, immediately before the demerger, become the liabilities of the resulting company by virtue of the demerger;
- (iii) the property and the liabilities of the undertaking or undertakings being transferred by the demerged company are transferred at values appearing in its books of account immediately before the demerger;
- (iv) the resulting company issues, in consideration of the demerger, its shares to the shareholders of the demerged company on a proportionate basis;
- (v) the shareholders holding not less than three-fourths in value of the shares in the demerged company (other than shares already held therein immediately before the demerger, or by a nominee for, the resulting company or, its subsidiary) become shareholders of the resulting company or companies by virtue of the demerger. Otherwise than as a result of the acquisition of the property or assets of the demerged company or any undertaking thereof by the resulting company;
- (vi) the transfer of the undertaking is on a going concern basis;
- (vii) the demerger is in accordance with the conditions, if any, notified under sub-section (5) of section 72A by the Central Government in this behalf.

For the purpose of this definition, “undertaking” shall include any part of an undertaking, or a unit or division of an undertaking or a business activity taken as a whole, but does not include individual assets and or liabilities or a combination of these not constituting a business activity. For determining the value of the property which is subject matter of demerger, any change in the value of assets on account of revaluation shall be ignored.

Splitting up or the reconstruction of any authority or a body constituted or established under any Act, or a local authority or a public sector company, into separate authorities or bodies or local authorities or companies shall be deemed to be the demerger if such split up or reconstruction fulfils the conditions as may be notified by the Central Government.

DEMERGED COMPANY SEC. 2(19AAA)

It means the company whose undertaking is transferred, pursuant to a demerger, to a resulting company.

DEFINITIONS

- **Undertaking** : includes any part of an undertaking or a unit or division of an undertaking or a business activity taken as a whole, but excludes individual assets or liabilities or combination of both not constituting a business activity.

Resulting Company : means one or more companies (including wholly owned subsidiary thereof) to which the undertaking of the demerged company is transferred in a demerger and the resulting company in consideration of such transfer of undertaking, issues shares to shareholders of the demerged company and includes any authority or body or local authority or public sector company or a company established, constituted or formed as a result of demerger

- **Provisions applicable to Company — Amalgamation/Demerger**

Capital Gain - Gains arising on transfer of a capital asset in a scheme of amalgamation/demerger to the amalgamated/resulting company being an Indian Company is exempt.

**Carry forward of accumulated loss and/or unabsorbed depreciation**

- Accumulated loss and unabsorbed depreciation of an amalgamating company owning an industrial undertaking or a ship or a hotel or a banking company can be transferred to the amalgamated company provided:
 1. it continuously holds 3/4th value of the assets acquired in a scheme of amalgamation for at least five years from the date of amalgamation.
 2. it continues to carry on business of amalgamating company for at least five years from the date of amalgamation and the amalgamating company.
- Accumulated loss and unabsorbed depreciation of a demerged company will be transferred to resulting company:
 1. Where it is directly relatable to undertaking transferred, it should be such relatable amount.
 2. Where it is not directly relatable to the undertaking transferred, it should be apportioned in the ratio of assets retained by the demerged company and transferred to resulting company.

Carry forward of accumulated loss and/or unabsorbed depreciation of the banking company in a Scheme of amalgamation with banking institution

Allowability of expenditure relating to amalgamation/demerger

- An Indian company will be allowed a deduction of 1/5th of the expenditure incurred for the purposes of amalgamation or demerger after 1st April, 1999 for five years from the years of amalgamation/demerger. (S. 35DD)

Depreciation in the year of amalgamation/demerger

- Depreciation to amalgamated company and amalgamating company in the year of amalgamation and depreciation to demerged company and the resulting company in the year of demerger shall be apportioned in the ratio of the number of days for which the assets were used (S. 32) (5th proviso).

Actual cost

- Actual cost of the capital asset transferred to amalgamated/resulting company shall be the actual cost in the hands of the amalgamating/demerged company provided it does not exceed WDV of such assets in the hands of the demerged company.

Written Down Value

- WDV in the hands of amalgamated company shall be the WDV of the block of assets in the hands of the amalgamating company less depreciation allowed in the year of amalgamation.
- WDV in the hands of the resulting company shall be the WDV of transferred assets as per books of the demerged company immediately before demerger.
- WDV in the hands of the demerged company shall be the WDV of the block of assets before demerger less book value of assets transferred to the resulting company.
- Deduction claimed under Section 33AC (Reserve for shipping business) would not be withdrawn on sale or transfer of a ship in any scheme of demerger.
- Transfer of patent rights or copyrights (S. 35A) or transfer of licence to operate telecommunication services (S. 35ABB) or transfer of business for prospecting etc. mineral oil (S. 42) in a scheme of amalgamation/demerger will not be treated as either sale or transfer.

- The deductions hitherto granted to amalgamating / demerged company relating to patent rights and copyrights (S. 35A) / Expenditure on know-how (S.35AB) / Licence fees to operate telecommunication services (S. 35ABB) / Preliminary expenses (S. 35D) / expenditure for prospecting etc., for certain minerals (S. 35E) / business for prospecting etc., for mineral oil (S. 42) would be available for balance period to the amalgamated / resulting company.

Provisions applicable to Shareholders

- Gains arising on transfer of shares of amalgamating company in exchange of shares of amalgamated company, being an Indian Company is exempt.
- Acquisition of shares of the resulting company by the shareholders in demerger will not be taxed either as capital gain or deemed dividend.
- Cost of acquisition of shares of :
 - the amalgamated company will be the cost incurred for acquiring shares of amalgamating company.
 - the resulting company will be the :
 - Original cost of shares of demerged company X net book value of assets transferred to resulting company / net worth of the demerged company before demerger (net worth is equal to Paid-up Share Capital + General Reserve as per books.)
 - the demerged company will be the original cost of shares of demerged company – cost of shares of the resulting company as computed above.

17.6 ASSESSMENT OF COOPERATIVE SOCIETIES

Introduction

Cooperative society is a society registered under the Cooperative Societies Act, 1912, or under any other law for the time being in force in any State for registration of cooperative societies.

A cooperative society is entitled, to some deduction u/s. 80P of the Income-tax Act.

Steps in computing tax liability of Cooperative Societies

The steps are-

- Step-I** : Compute gross total income, ignoring income exempt from tax u/s. 10 to 13A
- Step-II** : Deduct permissible deductions u/ss. 80G, 80GGA, 80I, 80I-A 80IB, 80JJA, etc. and 80P as applicable.
- Step-III** : Apply the tax rates for the relevant assessment year to arrive at the tax incidence.

The tax rates applicable are as follows :-

The rates of Income-tax are —

Income Range	Rates of tax
1. Where the total income does not exceed ₹ 10,000	10% of the total income
2. Where the total income exceeds ₹ 10,000 but which the does not exceed ₹ 20,000	₹ 1,000 plus 20% of the amount by total income exceeds ₹10,000
3. Where the total income exceeds ₹ 20,000	₹ 3,000 plus 30%, of the amount by which the total income exceeds ₹ 20,000

However, the tax payable by every cooperative society shall be increased education cess @2% and secondary and higher education cess @ 1%.



17.7 ASSESSMENT OF TRUSTS

Introduction

<i>Trust</i>	A "Trust" is an obligation annexed to the ownership of property, and arising out of a confidence reposed in and accepted by the owner, or declared and accepted by him, for the benefit of another, or of another and the owner.
<i>Author of trust</i>	The person who reposes or declares the confidence is called the "author of the trust".
<i>Trustee</i>	The person who accepts the confidence is called the "trustee".
<i>Beneficiaries</i>	The person for whose benefits the confidence is accepted is called the "beneficiary".

In order to ascertain the incidence of tax it is essential to know the nature and character of trusts and also the mode of computation of its income and conditions for exemptions. For the purpose of levy of income-tax, trusts may be of the following types :-

1. Charitable trust
2. Private discretionary trust
3. Oral trust

Charitable Trusts

A charitable trust is a trust established in accordance with law for charitable purpose. Charitable purpose includes relief of the poor, education, medical relief and the advancement of any other object of general public utility. [Sec. 2(15)]

Promotion of sports and games is considered to be a charitable purpose and as such an association or institution engaged in promotion of sports and games can claim exemption u/s.11, although it is not approved u/s. 10(23).

Conditions for exemption

The following essential conditions are to be fulfilled for claiming exemption u/s. 11 :-

- (i) The property from which income of the trust is derived should be held for charitable or religious purposes.
- (ii) The exemption is confined to such portion of the trust's income as is applied to charitable or religious purposes in India except in cases enumerated in sec.11(1)(c)
- (iii) If the trust property comprises of a business undertaking, the income shown in the books of account should not be less than the income determined by the A.O. according to provisions of the Income-tax Act. From A.Y. 1992-93, trusts or institution can carry out business activities if such business activities are incidental to the attainment of its objectives and separate books of accounts are maintained.
- (iv) The trust should make an application in Form No. 10A to the Commissioner of Income Tax within one year of creation of trust or the institution and such trust or institution get registered u/s. 12AA.
- (v) Limit for audit of charitable institutions rationalized [Section 12A]
 - Trusts and institutions covered under sections 11 and 12 to get their accounts audited only when their total income, before giving effect to the provisions of sections 11 and 12, exceeds ₹1,00,000.
- (vi) The funds of the trust should be invested or deposited in any one or more of the modes or forms [Sec. 11(5)] such as —
 - investment in Government Savings Certificate;
 - deposits in any Post Office Savings Bank Account;
 - deposit in any account with any scheduled or cooperative Bank;
 - investment in any Central Government or State Government securities or in the units of the Unit Trust of India;
 - investment in debentures of any corporate body, guaranteed by the Central Government or a State Government ;

- investments in immovable property or deposit in any public sector company ;
- deposit or investments in any Bond issued by a public company having main object of carrying on business of providing long term finance for urban infrastructure in India.
- any other form or mode of investment/deposit as may be prescribed in this behalf.

In order to claim exemption, a charitable trust or institution will have to apply at least 85% of, the income to charitable and religious purposes. Where 85% of the income is not applied to charitable or religious purposes the trust or institution may accumulate or set apart either the whole or part of its income for future application for such purposes in India.

Special rates of tax on Certain Income of Charitable Institutions.

Taxation of certain anonymous donations under section 115BBC

Income of wholly or partly charitable or religious trust etc. is exempt subject to certain conditions:

Unaccounted contribution to those institutions by way of anonymous donation a new section 115BBC has been inserted so as to provide that any income by way of anonymous donation shall be included in the total income and taxable @ 30%.

Note :

Anonymous donation means any voluntary contribution referred to sec 2(24)(iia).

Tax relief on anonymous donations for partly religious and partly charitable institutions, and wholly charitable institutions (Section 115BBC) [W.e.f. A.Y. 2010-11]

- (A) Under the current provisions of section 115BBC, wholly religious entities are outside the purview of taxation of anonymous donations. Partly religious and partly charitable entities have also been, exempted from the taxation of anonymous donations, except where the anonymous donation is made to an educational or medical institution run by such entity in which case such donations are taxed at the rate of 30%. In the case of wholly charitable entities, all anonymous donations are taxed at the rate of 30%.

In order to mitigate the compliance burden, the Act has provided relief to such organizations by exempting a part of the anonymous donations from being taxed. The amendment will result in the following:

1. Anonymous donations received by wholly religious institutions shall remain exempt from tax.
 2. In the case of partly religious and partly charitable institutions, anonymous donations directed towards a medical or educational institutions run by such entities shall be taxable @ 30% on the aggregate of anonymous donation received in excess of the higher of the following, namely:—
 - (A) 5% of the total donations received by the assessee, or
 - (B) ₹ 1,00,000.
 3. In the case of wholly charitable institutions, anonymous donations shall be taxable @ 30% on the aggregate of anonymous donation received in excess of the higher of the following, namely
 - (B) 5% of the total donations received by the assessee, or
 - (C) ₹ 1,00,000.
- (B) Meaning of charitable purpose' amended: See para 2 above.

Forfeiture of Exemption [Sec. 13]

The following incomes of charitable or religious trusts and institutions will not qualify for exemption u/s. 13 :-

- (i) income from property held under a trust for private religious purpose which does not ensure for the benefit of the public. [sec. 13(1)(a)]
- (ii) income of a charitable trust/institution established on or after 1.4.1962 for the benefit of any particular religious community or caste. [sec. 13(1)(b)]
- (iii) income of religious/charitable trust/institutions established after 31.3.1962 for the benefit of any person specified in sec. 13(3) viz. author, founder or substantial contributor of the trust or any relative of them.



Where the income is used or applied during the relevant year for the direct or indirect benefit of the above mentioned persons. [sec. 13(1)(c)(i) and (ii)]

- (iv) income of a trust/institution, if its funds are invested/deposited otherwise than as specified u/s. 11(5). [sec. 13(1)(d)]

However, the provisions of section 13(1)(d) shall not apply in relation to following :-

- any asset forming part of the corpus of the trust as on 1.6.1973;
- any accretion to the corpus shares by way of bonus shares allotted to the trust;
- debentures issued by or on behalf of any company or corporation and acquired by the trust before March 1, 1983;
- any asset not covered u/s. 11(5) where such asset is held for not more than 1 year from the end of the previous year in which such asset is acquired;
- any fund representing the Profits and gains of business, being Profits and gains of any previous year relevant to the assessment year 1984-85 or any subsequent assessment year. But such relaxation of the restriction will be denied unless the trust keeps separate accounts for the business. As already noted, subject to certain exceptions, such business profits no longer enjoy exemption u/s. 11.

CHANGES RELATING TO INCOME OF CHARITABLE INSTITUTIONS.

Anonymous donations to form part of income of trust [section 13]

As per the new section 115BBC, anonymous donation shall now be taxable at the maximum marginal rate of 30%. Consequently, a new sub-section (7) has been inserted in section 13 to provide that nothing contained in section 11 or section 12 shall operate so as to exclude from the total income of the previous year of the person in receipt thereof, any anonymous donation referred to in the new section 115BBC on which tax is payable in accordance with the provisions of that section. In other words anonymous donation shall not be excluded from the total income of the assessee.

Taxation of Trust

A. Public Trust u/s. 164(2) —

- If income is not exempt u/s. 11 or 12, income of Trust is taxable at the rates applicable to an Association of Person.
- If the exemption is forfeited due to contravention of sec. 13(1)(c) or 13(1)(d), such income of trust is taxable at minimum marginal rate.

B. Private Trust (shares of beneficiaries are determinate or known) —

- If income does not include business Profits, the trustee is assessable at the rates applicable to each beneficiary. [Sec. 161(1)]
- If income includes profits from business, the whole income is taxable at maximum marginal rate. [Sec. 161(1A)]

C. Private Trust (share of beneficiaries in determinate or unknown) [S. 164(i)] —

- If income does not include business profits, income is taxable at the rates applicable to an AOP if –
 - none of the beneficiaries has taxable income or is a beneficiary in any other trust.
 - the trust is non-testamentary trust created before 1.3.1970.
 - exclusively for the relative dependents of the settlor; or

- it is the only trust declared by a WILL exclusively for the benefit of any dependent relative. In any other case, income is taxable at minimum marginal rate.

(ii) If income includes business profits, the whole income is taxable at maximum marginal rate.

D.Oral Trust [Sec. 160(1)(v), Sec. 164A] : “Oral Trust” means a trust which is not declared by a duly executed instrument in writing including any wakf deed which is valid under the Mussalman wakf validating Act, 1913 and which is not deemed to be trust by virtue of explanation I to Sec. 160.

- (i) Income of Oral trust is taxable at maximum marginal rate.
- (ii) If Oral trust is declared to be a trust by furnishing a statement in writing containing purposes, particulars and details of trust, beneficiaries and property to the assessing officer within 3 months from the date of declaration of the trust, indicating the share of beneficiaries, the income of the trust is assessable in the hands of trustee at the rates applicable to beneficiaries.

Income from property held under Trust Partly for religious purposes and partly for other purposes [Sec. 164(3)]

Where property is held under trust partly for religious purposes and partly for other purposes and the individual share of the beneficiaries in the income applicable to purposes other than charitable purposes, is not known, the income-tax liability will be aggregated as follows :

- (i) the tax which would be chargeable on the part of the relevant income which is applicable to charitable or religious purposes (as reduced by the income which is exempt u/s. 11 as if such part were the total income of an association of persons; and
- (ii) the tax on that part of income attributable to purposes other than charitable or religious and in respect of which shares of beneficiaries are indeterminate or unknown, at the maximum marginal rate.

Where any part of income is not exempt u/s. 11 or 12 by virtue of sec. 13(1)(c) or (d), tax is charged on the relevant income at the maximum marginal rate.

Taxation of non-resident Indian

- (i) **Who is non-resident individual** — Sec. 6 [refer to Study Note 1 of study material]
- (ii) **Who is non-resident Indian** — An individual who is a citizen of India or a person of Indian origin not resident in India, is called non-resident Indian.
- (iii) **Taxation of non-resident assessee**
 - Provisions as applicable to resident assessee.
 - Special provisions as provided in Sec. 115C to 115I.

The non-resident has an option to be assessed or not to be assessed under special provision for any assessment year. The option is to be exercised by a declaration in his return of Income for the Assessment Year. [Sec. 115-1]



(iv) General Provisions —

Rate of tax	Similar to resident assesseees.
	<p>Special rates of tax on Dividends, interest income from units of Mutual Fund. UTI, bonds or shares purchased in foreign currency and capital gains arising from their transfer.</p> <ul style="list-style-type: none"> • 20% of the dividends [which have not been subjected to additional Income Tax u/s 115-O] [other than dividends mentioned in clause (iv) below]; • 20% of the interest received from Government or an Indian concern on monies borrowed or debt incurred in foreign currency; • 20% of the income received in respect of units purchased in foreign currency, of a Mutual Fund specified u/s 10(23D) or of the Unit Trust India; • 10% of the interest or dividends [which have not been subjected to additional income tax u./s 115-O], in respect of bonds or Global Depository Receipts in an Indian company purchased in foreign currency and issued under the Foreign Currency Convertible Bonds and Ordinary shares (Through Depository Receipt Mechanism) Scheme, 1993 (commonly known as Euro Issues/Euro Bonds) or in respect of bonds or Global Depository Receipts issued against shares of a public sector company sold by the Government to the non-resident in foreign currency; and • 10% of the long-term capital gains arising from the transfer of the aforesaid bonds or Global Depository receipts.

(v) Filing of return — Similar to resident assesseees :

However, a non-resident shall not be required to file a return of income u/s. 139(1), if his total income consists only of income subject to special rates of tax as mentioned in rate of tax under clauses (iv) supra and the tax has been deducted therefrom at source.

Case Laws :

- For purpose of section 164(1) what is relevant is that income is receivable on behalf of beneficiaries and is not necessary that income is received by beneficiaries - *Gosar Family Trust v. CIT* 81 Taxman 146/215 ITR 55.
- Provision merely sets out how tax is to be charged and does not create a charge on the income. CIT v. Kamalini Khatau* 209 ITR 101.

ASSESSMENT OF AOP / BOI (Sec. 86)

The assessment of the members of AOP or BOI depends on whether the AOP or BOI is chargeable to tax at the maximum marginal rate or at slab rate or is not chargeable to tax at all.

Tax-treatment in the three cases is discussed below:

- (i) Where AOP or BOI is chargeable to tax at a maximum marginal rate or any higher rate, the share of profit of a member is exempt from tax. Thus, it is not to be included in the total income of the member [Sec. 86(a)]
- (ii) Where AOP or BOI is not taxed at the maximum marginal rate but it is taxed at slab rates, the share of profit of a member from AOP or BOI is to be included in the total income of the member only for rate purposes. The member is entitled to a rebate of tax on the entire share of profit at the average rate of tax applicable to total income. [Sec. 86(b)].
- (iii) Where AOP or BOI is not chargeable to tax at all, the share of profit of a member from AOP or BOI is included in his total income and he will pay tax on it. He is not entitled to any rebate of tax on such profits [Proviso to Sec. 86(b)].

ILLUSTRATIONS ON ASSESSMENT OF AOP / BOI

Illustration 1. A & B are members of AOP, sharing profit and losses in the ratio of 5 : 3 and they are allowed the following payments:

	A ₹	B ₹
(i) Salary	40,000	60,000
(ii) Interest on capital or loan	20,000	10,000

You are required to compute taxable business profits of AOP and share of each member for the previous year 2011-2012 in the following cases:

- (a) AOP has earned profit of ₹ 3,00,000 after making the above payments;
- (b) AOP has earned profit of ₹ 3,00,000 before making the above payments;
- (c) AOP has suffered loss of ₹ 3,00,000 after making the above payments; and
- (d) AOP has suffered loss of ₹ 3,00,000 before making the above payments.

Solution: Computation of income of AOP for the PY 2011-2012 :

Particulars ₹	Case (a) ₹	Case(b) ₹	Case (c) ₹	Case (d) ₹
Profit/ loss	(+) 3,00,000	(+) 3,00,000	(-) 3,00,000	(-) 3,00,000
Add: Inadmissible payments [Sec. 40 (ba)]:				
(i) Salary to members (40,000+60,000)	(+) 1,00,000	—	(+) 1,00,000	—
(ii) Interest on capital/loan to members: (20,000 + 10,000)	(+) 30,000	—	(+) 30,000	—
Profit/loss as per income-tax law	(+) 4,30,000	(+) 3,00,000	(-) 1,70,000	(-) 3,00,000

Computation of member's share in the income/loss of the AOP

Particulars	Case (a)		Case (b)		Case (c)		Case (d)	
	A ₹	B ₹	A ₹	B ₹	A ₹	B ₹	A ₹	B ₹
Salary	40,000	60,000	40,000	60,000	40,000	60,000	40,000	60,000
Interest	20,000	10,000	20,000	10,000	20,000	10,000	20,000	10,000
Divisible profit:								
(a) 4,30,000–1,30,000	1,87,500	1,12,500	X	X	X	X	X	X
(b) 3,00,000–1,30,000	X	X	10,6250	63750	X	X	X	X
(c) (–) 1,40,000 + (–) 1,30,000= (–) 2,70,000	X	X	X	X	(1,68,750)	(101250)	X	X
(d) (–) 3,00,000 + (–) 1,30,000= (–) 4,30,000	X	X	X	X	X	X	(2,68,750)	(161250)
Share of profit/loss	2,47,500	1,82,500	1,66,250	1,33,750	(108750)	(31250)	(208750)	(91250)

- (i) *Where assessed business income is a profit:* Beneficial payments (i.e. salary, bonus, commission and interest) made to partners should be deducted from assessed profit to arrive at divisible profit, which is to be apportioned among members.
- (ii) *Where assessed business income is a loss:* Beneficial payments made to partners should be added to assessed loss to arrive at the divisible loss which is to be apportioned among members.

Illustration 2. Anand and Aniket are equal members in AA & Associates. The profit and loss account of the AOP for the year ending 31st March 2012 is as follows:

Particulars	₹	Particulars	₹
Selling and administrative Expenses	8,00,000	Gross Profit	20,00,000
Interest to Anand @ 15% Remuneration:	60,000	Income from house property	3,60,000
Anand	1,50,000		
Aniket	1,50,000		
Net profit:			
Anand	6,00,000		
Aniket	6,00,000		
	<u>23,60,000</u>		<u>23,60,000</u>

Other information :

- Selling and administrative expenses include ₹ 60,000 paid to a consultant in cash.
- The other income/investment details of the members are given as below:

Members	Income	Source of income	Investments
Anand	90,000	Interest on fixed deposit from bank	Purchase of NSC VIII ₹ 30,000
Aniket	1,00,000	Interest on govt. securities	Contribution to PPF ₹ 50,000

Compute the tax liability of the AOP and its members.

Computation of total income of AOP: PY 2011-2012

Particulars	₹
Net profit	12,00,000
Add: Inadmissible payments.	
1. Fees paid to consultants in cash Sec. 40A (3)	60,000
2. Interest paid to members [Sec. 40(ba)]:	60,000
3. Remuneration paid to members Sec. 40(ba)	3,00,000
	<u>16,20,000</u>
Less: Income from house property	3,60,000
Business profits	12,60,000
Add: Income from house property	3,60,000
Total income	16,20,000
Tax liability of AOP on total income	
Tax on slabs rates	3,90,000
Add:	
Education cess 2%	7,800
SHEC @ 1%	3,900
Tax payable	4,01,700

Allocation of income amongst the members:

Particulars	Anand ₹	Aniket ₹	Total ₹
Interest	60,000	—	60,000
Remuneration	1,50,000	1,50,000	3,00,000
Share of divisible profit (12,60,000-60,000-3,00,000)	4,50,000	4,50,000	9,00,000
Share of profit	6,60,000	6,00,000	12,60,000
Share of income from house property	1,80,000	1,80,000	3,60,000
	<u>8,40,000</u>	<u>7,80,000</u>	<u>16,20,000</u>

Computation of total income of members:

Particulars	Anand ₹	Aniket ₹
Share income from AOP	8,40,000	7,80,000
Income from other sources:		
Interest on bank deposits	90,000	—
Interest on government securities	—	1,00,000
Gross total income	9,30,000	8,80,000
Less: Deduction under Sec. 80C	30,000	50,000
Total income	9,00,000	8,30,000
Tax liability of members : Tax on slab rates	1,74,000	1,53,000
Add: Education cess @ 2% on income tax	3,480	3,060
Add : SHEC @ 1%	1,740	1,530
	<u>1,79,220</u>	<u>1,57,590</u>
Less: Rebate on share of profit at the average: (See Note below)	1,67,272	1,48,097
Tax payable	11,948	9,493
Tax payable rounded off to the nearest multiple of ₹ 10 (Sec. 288B)	11,950	9,490
Note: Anand $\frac{1,79,220}{9,00,000} \times 8,40,000$ Aniket : $\frac{1,57,590}{8,30,000} \times 7,80,000$	15,050	12,290



Illustration 3. A, B and C Ltd. are three members of an AOP, sharing profit and losses in the ratio 2:2:1. The AOP discloses its income for the PY 2011-2012 as below:

Particulars	₹
(i) Long-term capital gains	4,00,000
(ii) Business profits	6,00,000

Determine tax liability of AOP in the following cases:

- C Ltd. is an Indian company
- C Ltd. is a foreign company

Solution: Allocation of income of AOP among partners

Particulars of income	A ₹	B ₹	C Ltd ₹
Long-term capital gains	1,60,000	1,60,000	80,000
Business profits	2,40,000	2,40,000	1,20,000
Share income of the members	4,00,000	4,00,000	2,00,000

Tax liability of AOP

Particulars	Case – I C Ltd. an Indian company ₹	Case – II C. Ltd. as foreign company ₹
Tax on the share of C Ltd. Case I : 1,20,000 × 33.99%	40,788	—
Case II: 1,20,000 × 42.23%	—	50,676
Tax on balance income at AOP:		
(i) Long-term capital gain 4,00,000 × 22.66%	90,640	90,640
(ii) Business profits 6,00,000 × 33.99%	2,03,940	2,03,940
Total tax payable	3,35,368	3,45,256
Total Tax (Rounded off a/c 288B)	3,35,370	3,45,260

Illustration 4. R, S and T Ltd. (a widely held domestic company) are members in an AOP for the previous year 2011-2012. They share profit and losses in the ratio 30%, 40% and 30%. Taxable business income of AOP is determined at ₹ 8,00,000. Personal income of the partners are given below:

	₹
R - House property	90,000
S – Short-term capital gain	1,00,000

R deposits ₹ 20,000 in CTDS-15-year account in Post Office in February 2010. S purchases NSC VIH-Issue for ₹ 25,000 in December 2011.

Determine the tax liability of the AOP and its partners

Solution : (a) Computation of tax liability of AOP for the previous year 2011-2012.

Allocation of AOP income among members:

Particulars	R ₹	Y ₹	T Ltd. ₹
Business profit	2,40,000	320000	240000

Tax liability of AOP: 8,00,000 × 33.99%

2,71,920

Tax liability of members:

Particulars	R ₹	Y ₹	T Ltd. ₹
Share income from AOP	2,40,000	320000	240000
AOP charged at maximum marginal rate	Exempt	Exempt	Exempt
Personal income of members	90,000	75,000	Nil
Personal income below taxable limit	Exempt	Exempt	X

Illustration 5. GMK are partners in a firm assessed as an association of persons. They share profit and losses in the ratio of 4:3:3. The abridged profit and loss for the previous year 2011-2012 is as follows:

Particulars	₹	Particulars	₹
Business expenses	5,00,000	Gross profits	6,85,000
Salaries to partners		Short-term capital gain	2,80,000
G	60,000	Interest on drawings	
M	40,000	G	5,000
K	50,000	M	20,000
Bonus to partners:		K	10,000
G	30,000		
M	20,000		
Commission to K	40,000		
Interest to partners:			
G	20,000		
M	15,000		
K	25,000		
Net profit			
G	80,000		
M	60,000		
K	60,000		
	10,00,000		10,00,000

Business expenses include donation to Nalanda University ₹ 50,000.

Compute the taxable income of AOP, its tax liability and tax liability of its members in the following

Personal income of members	Case-I ₹	Case-II ₹
G: Interest on bank deposits	40,000	1,00,000
M: Interest on government securities	65,000	1,20,100
K: Income from house property	50,000	1,10,000
LIP paid by every member on a policy of ₹ 1,00,000.	20,000	20,000

Solution : (a) Computation of Taxable Business Profits

Particulars	₹
Net profit as per Profit & Loss A/c	2,00,000
Add: (i) Donation to Nalanda University	50,000
(ii) Salaries to partners [Sec. 40(ba)] (60,000 + 40,000 + 50,000)	1,50,000
(iii) Bonus to partners 30,000 + 20,000	50,000
(iv) Interest on capital (Net of Interest on Drawings)	15,000
G 20,000 – 5,000 =	15,000
K 25,000 – 10,000 =	15,000
(v) Commission to K	<u>40,000</u>
	5,20,000
Less: Short-term capital gain	<u>2,80,000</u>
Taxable profits	
(a) Computation of total income	
Add: (i) Business profits	2,40,000
(ii) Short-term capital gain	<u>2,80,000</u>
Gross total income	5,20,000
Less: Deduction for charitable donation (Sec. 80G)	
(a) Actual donation ₹ 50,000 or,	
(b) 10% of gross total income: $\frac{10}{100} \times 5,20,000 = 52,000$	
whichever is less, is qualifying amount. It is ₹ 50,000.	25,000
Amount of deduction 50% of qualifying amount	
Total income	<u>4,95,000</u>

Tax liability of AOP :

Particulars	Case I	Case II
(a) Tax on total income at slab rates including Education Cess and SHEC	1,00,425	—
(b) Tax on total income at maximum marginal rates including surcharge plus education cess plus SHEC	—	1,68,251
Tax payable	1,00,425	1,68,251
Tax payable rounded off (u/s 288 B)	1,00,420	1,68,250

Tax liability of members:

Case:(a) where AOP is taxed at slab rates:

Share of income from AOP:	G (₹)	M (₹)	K (₹)	Total (₹)
(i) Salary	60,000	40,000	50,000	1,50,000
(ii) Bonus	30,000	20,000	—	50,000
(iii) Commission	—	—	40,000	40,000
(iv) Interest	15,000	—	15,000	30,000
	1,05,000	60,000	1,05,000	2,70,000
(v) Divisible loss : (2,40,000-25,000)-270,000 = (-) 55,000	(-) 22,400	(-) 16,500	(-) 16,500	(-) 55,000
Share of business profit	83,000	43,500	88,500	2,15,000
Share of short-term capital gain	112,000	84,000	84,000	2,80,000
Share of income from AOP	1,95,000	1,27,500	1,72,500	4,95,000

Total Income and Tax Liability of members :

Particulars	G	M	K
Income from house property	—	—	50,000
Income from other sources	40,000	65,000	—
Share income from AOP:	1,95,000	1,27,500	1,72,500
Gross Total Income	2,35,000	1,92,500	2,22,500
Less: Deduction under Sec. 80C: LIP restricted to 20% of policy	20,000	20,000	20,000
Total Income	2,15,000	1,72,500	2,02,500
Gross income tax at slab rate	17,000	8,500	10,500
Add: Surcharge	Nil	Nil	Nil
Add: Education Cess @ 2%	340	170	210
Add : SHEC @ 1%	170	85	105
	17,510	8,755	10,815
Less: Rebate on share of profit from firm at the average rate	15,881	6,471	9,213
Tax payable	1,629	2,284	1,602
Tax payable rounded off (u/s 288B)	1,630	2,280	1,600
Note 1: $17,510 \div 2,15,000 \times 1,95,000 = 15,881$			
Note 2: $8,755 \div 1,72,500 \times 12,75,000 = 6,471$			
Note 3: $10,815 \div 2,02,500 \times 1,72,500 = 9,213$			



Case (b) where AOP is taxed at maximum marginal rate:

1. Share of profit from AOP; Since the AOP was assessed at the maximum marginal rate, share of income from AOP is exempt (Sec. 86)	G —	M —	K —
2. Personal income:			
Income from other sources	1,00,000	1,20,100	1,10,000
Less: Deduction u/s 80C	(-) 20,00	(-) 20,000	(-) 20,000
Total Income	80,000	1,00,100	90,000
	Nil	Nil	Nil
Total Income	Nil	Nil	Nil

Illustration 6. T and Q are individuals, who constitute an association of persons, sharing profit and losses in the ratio of 2:1. For the accounting year ending 31st March 2012, the profit and loss account of the business was as under:

Particulars	Rupees in thousands	Particulars	Rupees in thousands
Cost of goods sold	6,250.00	Sales	9,900.00
Remuneration to:		Dividend from companies	25.00
T	130.00		
Q	170.00	Long-term Capital gains	1,640.00
Employees	256.00		
Interest to :			
T	48.30		
Q	35.70		
Other expenses	111.70		
Sales-tax penalty due	39.00		
Net profit	4,524.30		
	11,565.00		11,565.00

Additional information furnished:

(i) Other expenses included:

- entertainment expenses of ₹ 35,000;
- wristwatches costing ₹ 2,500 each were given to 12 dealers, who had exceeded the sales quota prescribed under a sales promotion scheme;
- employer's contribution of ₹ 6,000 to the Provident Fund was paid on 14th January 2012.
- ₹ 30,000 was paid in cash to an advertising agency for publicity.

(ii) Outstanding sales tax penalty was paid on 15th April 2012. The penalty was imposed by the sales tax officer for non-filing of returns and statements by the due dates.

(iii) T and Q had, for this year, income from other sources of ₹ 3,50,000 and ₹ 2,10,000, respectively.

Required to :

- Compute the total income of the AOP for the previous year 2011-2012.
- Ascertain the tax liability of the Association for that year; and
- Ascertain the tax liability for that year of the individual members.

Solution : (a)(i) Computation of total income of the AOP for PY 2011-2012

Particulars	₹	₹
Profit and gains of business (see Working Note below)		33,12,300
Long term capital gain		16,40,000
Income from other sources [dividend is exempt u/s 10(34), assuming it is from domestic companies]		
Total income		49,52,300
Computation of profits and gains of business:		
Net profit as per profit and loss account		45,24,300
Add: Inadmissible payments:		
Interest to members T & Q (₹ 48,300 + ₹ 35,700)	84,000	
Advertising [disallowance u/s 40A(3)]	30,000	
Remuneration to members T & Q (₹ 1,30,000 + ₹ 1,70,000)	3,00,000	
Sales tax penalty due (See Note 3 below)	39,000	4,53,000
		49,77,300
Less : Income not taxable under this head		
Dividend from companies	25,000	
Long term capital gain	16,40,000	16,65,000
Profits and gains of business		33,12,300

(ii) Computation of tax liability of the AOP for PY 2011-2012

Particulars	₹	₹
Long-term capital gain (₹ 16,40,000 × 20%)		3,28,000
Other income (₹ 33,12,300 × 30%)		9,93,690
Tax on total income		13,21,690
Add : Education cess @ 2%		26,434
Add : SHEC @ 1%		13,217
Total tax due		13,61,341
Total Tax Rounded off (u/s 288B)		13,61,340

Note :

1. Since one of the members has individual income more than the basic exemption limit, the AOP will be assessed at the maximum marginal rate. The maximum marginal rate includes the surcharge applicable in relation to the highest slab of income in case of an individual and as such surcharge shall be chargeable at the rate of 10%.
2. Since the employer's contribution to PF has been paid during the previous year 2011-2012 itself, it is allowable as deduction.
3. Penalty imposed for delay in filing sales tax return is not deductible since it is on account of infraction of the law requiring filing of the return within the specified period.

(iii) Computation of Tax Liability of members T & Q for the PY 2011-2012

Particulars	₹	Particulars	₹
Tax on ₹ 3,50,000	54,000	Tax on ₹ 2,10,000	16,000
Add : Surcharge	Nil		Nil
	54,000		16,000
Add : Education cess @ 2%	1,080		320
Add : SHEC @ 1%	540		160
Net Tax Payable	55,620		16,480



ILLUSTRATIONS ASSESSMENT OF CHARITABLE TRUSTS

Illustration 1. Shri Dubbawala Charitable Trust (Regd.) submits the particulars of its income/outgoing for the previous year 2011-2012 as below :

	₹
(i) Income from property held under trust for charitable purposes: (₹ 5,20,000 out of ₹ 10,00,000 is received in PY 2012-2012)	10,00,000
(ii) Voluntary contributions (out of which ₹ 50,000 will form part of the corpus)	2,00,000

The trust spends ₹ 2,77,500 during the previous year 2011-2012 for charitable purposes. In respect of ₹ 5,20,000, it has exercised its option to spend it within the permissible time-limit in the year of receipt or in the year, immediately following the year of receipt.

The trust spends ₹ 2,00,000 during the previous year 2010-2011 and ₹ 1,00,000 during the previous year 2012-2013. Compute and discuss the chargeability of the income of the trust.

Solution : (a) Computation of taxable income and tax liability of the charitable trust for the PY 2011-2012/AY 2012-2013

Particulars	₹
(i) Income from property held under trust for charitable purposes	10,00,000
(ii) Voluntary contributions (₹ 2,00,000 - ₹ 50,000)	1,50,000
	11,50,000
Less: 15% set apart for future application	1,72,500
Balance	9,77,500
Less: Amount spent during the pervious year for charitable purposes	2,77,500
Balance	7,00,000
Less: Income not received during the previous year 2011-2012	5,20,000
Taxable income	1,80,000
Tax payable:	
1,10,000	Nil
40,000	10%
30,000	20%
	10,000
Add: Education Cess @ 2%	200
Add: SHEC @ 1%	100
	10,300
(b) Previous year 2012-2013/AY 2013-2014	
Income received during the pervious year 2011-2012	5,20,000
(i) Amount spent for charitable purposes during PY 2011-2012	2,00,000
(ii) Amount spent for charitable purposes during 2012-2013	1,00,000
Taxable income	2,20,000

Illustration 2. Shri Mungeri Ram Temple Trust (Regd.) derived ₹ 6,00,000 income from the property held under charitable trust during the pervious year 2011-2012. About 40% of the income has been received by the end of the financial year. The trust could spend ₹ 60,000 for charitable purposes during the year 2011-2012 and 40% receipts, received by the year end in 2011-2012, are being planned to be applied for charitable purposes during the previous year 2012-2013. Compute its income for the said two years if the amount planned to be spent during previous year 2012-2013 for charitable purposes is ₹ 1,00,000.

Solution : (a) Computation of taxable income of charitable trust: PY 2011-2012/AY 2012-2013.

Particulars	₹
Income from property held under trust	6,00,000
Less: 15% set apart for future application for charitable purposes	90,000
Balance	5,10,000
Less : Income applied for charitable purposes during the year 2011-2012	60,0000
Balance	4,50,000
Less: Income realised by the close of the previous year—40% of ₹ 6,00,000	2,40,000
Taxable income	2,10,000
(b) Previous year : 2010-2011 / AY 2011-2012	
Amount set apart in 2011-2012 to be applied for charitable purposes in 2012-2013 = 2,40,000	
Less: Amount applied for charitable purposes	= 1,00,000
Taxable Income	1,40,000

Illustration 3. Devdas Charitable Trust submits the particulars of its receipts and outgoing during the previous year 2011-2012.

as below :

	₹
(i) Income from property held under trust for charitable purposes	20,00,000
(ii) Voluntary contribution (out of which ₹ 5,00,000 will form part of the corpus)	15,00,000
(iii) Donations paid to blind charitable school	6,00,000
(iv) Scholarship paid to poor students	4,00,000
(v) Amount spent on holding free eye camps in urban slums	3,00,000
(vi) Amount set apart for setting up an old age home by March 2014	10,00,000

Compute the total income of the trust for the previous years 2010-2011 and 2015-2016 if it spends ₹ 5,00,000 during the previous year 2014-2015 and ₹ 3,00,000 during the previous year 2015-2016 in setting up the old age home.

Solution : (a) Computation of the Taxable Income of the trust for previous year 2011-2012/AY 2012-2013.

Particulars		₹
(i) Income from property held under charitable trust		20,00,000
(ii) Income from voluntary contributions (₹ 15,00,000-₹ 5,00,000)		10,00,000
Total		30,00,000
Less : 15% set apart for future application		45,00,000
Balance		25,50,000
Less: Income applied for charitable purposes:		
(i) Donations to blind charitable school	6,00,000	
(ii) Scholarship to poor students	4,00,000	
(iii) Free eye camps in urban slums	3,00,000	
Total	13,00,000	
Amount set apart for old age home	10,00,000	23,00,000
Taxable Income		2,50,000
(b) Previous year 2015-2016 / AY 2016-2017:		
Amount set apart for old age home	10,00,000	
Less : 1. Amount spent during 2014-2015	3,00,000	
2. Amount spent during 2015-2016	5,00,000	
Taxable Income	2,00,000	



Illustration 4. CD Charitable Trust furnishes the following particulars, for the year 2011-2012:

(i) Sale price of capital assets	15,30,000
(ii) Expenses incurred in connection with sale of the asset	30,000
(iii) Cost of the asset sold (purchased in 2010-2011)	5,00,000
(iv) Compute capital gain in the following cases:	
(a) Cost of the new asset to be acquired	15,00,000
(b) Cost of the new asset to be acquired	8,00,000
(c) Cost of the new asset to be acquired	4,00,000

Solution: Computation of capital gain: PY 2011-2012/AY 2012-2013

Particulars	Case-I ₹	Case-II ₹	Case-III ₹
Sale price Less:	15,30,000	15,30,000	15,30,000
(i) Selling expenses	(-) 30,000	(-) 30,000	(-) 30,000
(ii) Cost of the asset Short-term capital gain	(-) 5,00,000	(-) 5,00,000	(-) 5,00,000
	10,00,000	10,00,000	10,00,000
Less: Exemption in respect of capital gain	10,00,000	3,00,000	Nil
Taxable capital gain	Nil	7,00,000	10,00,000

- Note :**
1. Cost of new asset - cost of asset sold: 8,00,000 - 5,00,000 = 3,00,000
 2. Cost of new asset - cost of asset sold: 4,00,000 - 5,00,000 = Nil

ILLUSTRATIONS ASSESSMENT OF COOPERATIVE SOCIETIES

Illustration 1. Dinesh Pally Cooperative Society Ltd. furnishes the following particulars of its income for the previous year ending on 31st March 2012:

(i) Interest on government securities	40,000
(ii) Profits from banking business	3,50,000
(iii) Income from purchase and sale of agricultural implement and seeds to its members	2,50,000
(iv) Income from marketing of agricultural produce of its members	4,00,000
(v) Profits and gains of business	2,20,000
(vi) Income from cottage industry	3,50,000
(vii) Interest and dividends (gross) from other cooperative societies	30,000

Compute total income of the society and calculate the tax payable by it for the assessment year 2012-2013.

Solution : Dinesh Pally Cooperative Society Ltd.

Computation of income of the for the previous year 2011-2012 relating to the Assessment Year 2012-2013 :

Particulars	₹	₹
1. Profits and gains of business or profession:		
a) Banking business	3,50,000	
b) Income from purchase and sale of agricultural implements and seeds to its members	2,50,000	
c) Income from marketing of agricultural produce of its members	4,00,000	
d) Profits and gains of business	2,20,000	
e) Income from cottage industry	3,50,000	
		15,70,000
2. Income from other sources:		
a) Interest on government securities	40,000	
b) Interest and dividends from other cooperatives	30,000	
		70,000
Gross Total Income		16,40,000
Less: Deduction allowable from gross total income under Sec. 8OP		
1. Banking business	3,50,000	
2. Income from purchase and sale of agricultural implement and seeds to its members	2,50,000	
3. Income from marketing of agricultural produce of its members	4,00,000	
4. Income from cottage industry	3,50,000	
5. Interest on government securities(not eligible for deduction)	Nil	
6. Interest and dividends from other cooperative societies	30,000	
		13,80,000
Total Income		2,60,000



Computation of Tax Liability :

Particulars	Rate	₹
On first ₹ 10,000	10%	1,000
On next ₹ 10,000	20%	2,000
On balance ₹ 2,40,000	30%	<u>72,000</u>
Income tax payable		75,000
Add: Education cess @ 2%		1,500
Add: SHEC @ 1%		750
Tax payable		77,250

Illustration 2. A co-operative society, engaged in the business of banking, seeks your opinion by the matter of eligibility of deduction under Sec. 80P on the following items of income earned by it during the year ending 31-3-2012.

- Interest on investment in government securities made out of statutory reserves
- Hire charges of safe deposit lockers.

Answer : From the assessment year 2008-2009 and onward, no deduction is allowed under Sec. 80P to any cooperative bank. However, a primary agricultural credit society or primary cooperative agricultural and rural development bank is outside the purview of this provision [Sec. 80P(4)].

Illustration 3. A cooperative society was engaged in the business of banking or providing credit facilities to its members. It sold goods on credit to its members. Is the cooperative society entitled to special deduction under Sec. 80P(2)(a)(i) in respect of income derived from such an activity?

Answer : Society is not entitled to the special deduction under Sec. 80P(2)(a)(i).

ILLUSTRATIONS ASSESSMENT OF HUF

Computation of Tax-liability of an HUF :	₹
1. Gross income tax on its total income at the prescribed rates as aforesaid:	
(a) Gross income tax on winnings under [Sec. 115BB]	xxx
(b) Gross income tax on long-term capital gains [Sec. 112(1)]	xxx
(c) Gross income tax on short-term capital gain (Sec. 111A)	xxx
(d) Gross income tax on the balance of total income	xxx
Total gross income tax	xxx
2. Less: Rebate from gross income tax under Sec. 88E	xxx
Net income tax	xxx
3. Add: Surcharge on income tax	xxx
4. Add: Education surcharge @ 2% on the aggregate income tax and surcharge	xxx
5. Add: SHEC @ 1%	xxx
Total tax (3 + 4+ 5)	xxx
6. Less :	
(a) Rebate on share of profit from AOP under Sec. 86 where AOP (association of person) has been taxed at normal rate	xxx
(b) Relief under Sec. 89(1)	xxx
(c) Double taxation relief under Sec. 91	xxx
Tax due from an HUF	
Less: Prepaid taxes:	
(a) Tax deducted at source	xxx
(b) Advance payment of tax	xxx
(c) Tax paid on self-assessment under Sec. 140A	xxx
Tax payable/refund due to the assessee	
Tax payable is rounded off to the nearest multiple of ₹ 10 (Sec. 288B).	xxx

Illustration 1. The following details have been supplied by the Karta, of an HUF aged 62 years. You are required to compute its total income and tax liability for the assessment year 2012-2013.

Particulars	₹
(i) Profits from business (after charging ₹ 1,00,000 salary to Karta for managing the business).	15,00,000
(ii) Salary received by the member of a family.	60,000
(iii) Director's fee received by Karta from B Ltd where HUF holds 20% shares but he became director because of his qualifications,	40,000
(iv) Rental income from house property (after deduction of municipal taxes ₹ 2,000).	78,000
(v) Dividends (gross) from Indian companies	15,000
(vi) Long-term capital gain	80,000
(vii) Short-term capital gain	30,000
(viii) Donation to a school, which is an approved institution,	1,00,000
(ix) Deposits in Public Provident Fund	20,000
(x) NSC-VIII issues purchased	40,000

Solution: Computation of Total Income for the A.Y. 2012-13

Particulars	₹	₹
(i) Income from house property: Gross annual value (₹ 78,000 + ₹ 12,000) Less: Municipal taxes paid Annual value Less: Statutory deduction: 30% × 78,000	90,000 <u>12,000</u> 78,000 <u>23,400</u>	54,600
(ii) Profits and gains from business		15,00,000
(iii) Capital gains (a) long-term + (b) short-term		1,10,000
(iv) Income from other sources—gross dividends from Indian companies: Exempt [Sec. 10(34)]		Nil
Gross Total Income		16,64,600
Less:		
1. Contribution to approved savings (Sec. 80C)		
(i) Deposits in Public Provident Fund	20,000	
(ii) NSC-VIII Issue	<u>40,000</u>	60,000
2. Donation to recognised school:		
(a) Actual donation: ₹ 1,00,000 or		
(b) 10% of adjusted total income = (Gross Total Income – Long Term Capital Gains – All deductions under Chapter VIA excluding Sec. 80G) of ₹ 15,24,600 (16,64,600 - 80,000 - 60,000) whichever is less, is qualifying amount.		
Amount of deduction: : 50% of ₹ 1,00,000	<u>50,000</u>	<u>1,10,000</u>
Total Income		15,54,600

Computation of Tax Liability:

Particulars of total income	Rate of income tax		₹
	₹	₹	
(a) Long-term capital gain	80,000	20%	16,000
(b) Balance of total income: ₹ 14,74,600			
(i) First	2,50,000	Nil	—
(ii) Between 2,50,000 – 5,00,000	2,50,000	10%	25,000
(iii) Between 5,00,000 – 8,00,000	3,00,000	20%	60,000
(iv) Between 8,00,000 – 14,74,600	6,74,600	30%	2,02,380
Gross Income Tax			3,03,380
Add: Education cess @ 2% on income tax			6,068
SHEC @ 1% on income tax			3,034
Tax payable			3,12,482
Rounded off u/s 288B			3,12,480

Illustration 2. Prem was the Karta of HUF. He died leaving behind his major son Anand, his widow, his grandmother and brother's wife. Can the HUF retain its status as such or the surviving persons become co-owners?

Answer: Income-tax law does not require that there should be at least two male members to constitute an HUF [Gowli Buddanna CIT (1966) 60ITR 293 (SC)]. The expression "Hindu undivided family" used in the Act, should be understood in the sense in which it is understood under the Hindu personal law. The expression "Hindu undivided family" under the Income-tax Act is known as "joint Hindu family", under the Hindu personal law. A 'Joint family' may consist of a single male member and the widows of the deceased male members. The property of the Hindu joint family does not cease to be an HUF property merely because that the HUF, consist of one male member at a given point of time, exercising the proprietary rights over the property of HUF property.

Illustration 3. J (HUF) was the owner of a house property, which was being used for the purposes of a business carried on by a partnership firm JC & Co. in which the Karta and other members of the HUF were partners in their individual capacity. The Assessing Officer proposes to assess the annual letting value of the said property as the HUF's income from house property. The HUF contends that the building was used for business purposes and, therefore, the annual letting value thereof was not taxable in its hands as income from house property under Sec. 22. Examine the rival contention.

Answer: Section 22 directs not to tax the annual value of a house property which is used by the owner for his business profession, the profits of which are chargeable to tax. In the instant case, the HUF is not using its property for its business. The Karta of the Hindu undivided family and other members of the HUF are partners in the firm in their personal capacity. They have not joined the partnership on behalf of the HUF. Therefore, it cannot be said that the HUF property was being used by the HUF for its business. Hence, the Assessing Officer is justified to tax the income of the HUF property as income from "house property".

Illustration 4. J.Hazra was the Karta of a Hindu undivided family which was assessed to income tax. He died in an air crash and his two sons received ₹ 8 lakhs as compensation and ₹ 6 lakhs from the insurance company. The said amount of ₹ 14 lakhs was invested in units. The assessee claims that the income from these units is assessable as income of the Hindu undivided family composed of his sons and their families. Discuss.

Answer: The right to receive compensation and insurance claim did not vest in the assessee during his life-time. It came into existence only after his death. The income from investment and compensation would be personal income of the assessee [CIT v. L. Bansidhar & Sons (1980) 123 ITR 58 (Del.)].

Illustration 5. C, the Karta of a Hindu undivided family, was appointed as the treasurer of a private sector bank on his furnishing security of the family property valued at ₹ 3,00,000, as required by the service rules of the bank. C does not own any self-acquired property.

- (i) Discuss how the remuneration of C as the treasurer should be assessed.
- (ii) Will your answer be different if C had joined a partnership firm as a partner by contributing family funds of ₹ 30,000.

Answer:

- (i) Remuneration from bank cannot be treated a return on the security of family property, pledged with the bank to secure the continuity of service. It cannot be treated as income of the HUF.
Remuneration is a compensation for services rendered by C, in his personal capacity on account of personal qualifications. C is assessable on remuneration as income from "salary". He can claim standard deduction under Sec. 16.
- (ii) Membership of partnership has been obtained because of HUF funds and not because of personal skill or qualification of C. Therefore, any income from partnership firm will be treated as income of the HUF.



ILLUSTRATIONS ASSESSMENT OF COMPANIES

Illustration 1. From the following information, determine the tax liability of Z Ltd., domestic company, for the assessment year 2011-2012 and 2012-2013.

S. No.	Assessment year	Book-profits (₹)	Total income (₹)
1.	2011-2012	2,80,000	1,30,000
2.	2012-2013	3,00,000	2,00,000

Solution :

Surcharge is not considered assuming, net income less than Rs. 1 crore

Assessment year	Book-profit	Total Income	Tax on Book-Profit	Tax on Total Income @ 30.9% rounded off u/s 288B	Tax Credit = Tax on Book Profits (-) Tax on Total Income	Tax Payable after tax credit set off, if any	Tax credit balance
	₹	₹	₹	₹	₹	₹	₹
2011-2012	2,80,000	1,30,000	@ 18.54% on 2,80,000 = 51,912	@ 30.9% on 1,30,000 = 40,170	11,742	51,912	11,742
2012-2013	3,00,000	1,50,000	@ 19.055% on 3,00,000 = 57,165	@ 30.9% on 2,00,000 = 61,800	—	50,058 [61,800 – 11,742]	—

Note : Tax payable is rounded off to the nearest multiple of ₹ 10 (Sec. 288B)

Illustration 2. Fashion Ltd., a well-diversified group, gives below its profit and loss account for the previous year 2011-2012:

Particulars	₹	Particulars	₹
Manufacturing expenses	9,00,000	Sale of manufactured goods	10,00,000
Salaries/wages	5,50,000	Sale of agriculture produce	15,00,000
Cultivation expenses	4,00,000	Receipt from generation/distribution of power	15,00,000
Power generation/distribution expenses	4,00,000	Receipt from water supply/ irrigation projects	
Irrigation expenses	6,00,000	Receipt from I.U. set up in backward district in July 2004	10,00,000
Expenses of I.U., located in backward district	5,00,000	Transfer from Reserve & Provision a/c, debited to profit and loss account in 2005-06 on account of free service under warranty period	9,50,000
Expenses of I.U., located in free trade zone (Sec. 10A)	1,50,000	Sale of goods of I.U. (Sec. 10B)	2,00,000
Expenses of I.U. (Sec. 10B)	1,00,000	Sale of goods of I.U., located in free trade zone (Sec. 10A)	2,00,000
Expenses of I.U. (Sec. 10C)	50,000	Sale of goods of I.U. located in Northern Eastern Region (NER) (Sec. 10C)	1,00,000
Provision for losses of subsidiary	4,00,000	Income from UTI	50,000
Sundry expenses	10,000		5,00,000
Provision for bad and doubtful debts	2,00,000	Long term capital gain on sale of equity shares, transaction chargeable to Securities Transaction Tax	35,00,000
Provision for bills under discount	50,000		
Provision for sales tax, wealth tax against demand notice	3,30,000		
Income tax provision against demand notice	3,00,000		
Dividend paid on preference shares	2,00,000		
Proposed dividend on equity shares	4,00,000		
Transfer to general reserve	1,00,000		
Dividend Equalisation reserve	2,00,000		
Penalties under direct tax laws	60,000		
Goodwill written off	50,000		
Depreciation	3,00,000		
Amortisation of patent rights	30,000		
Expenses on transfer of equity shares	20,000		
Net profit	42,00,000		
	1,05,00,000		1,05,00,000

The following additional information is provided as below:

1. Depreciation includes, a sum of ₹ 1,00,000 on account of revaluation of building and plant and machinery.
2. Past year losses, before depreciation, are given below:

	Loss (₹)	Depreciation (₹)
2007-2008	(-) 5,00,000	(-) 6,00,000
2008-2009	Nil	(-) 5,00,000
2009-2010	(-) 7,00,000	(-) 4,00,000
2010-2011	(-) 5,00,000	Nil

Compute book-profits for the previous year 2011-2012/AY 2012-2013 for MAT under Sec. 115 JB.

Computation of Book Profit for the AY 2011-2012

Particulars	₹	₹
Net profit as per profit and loss account		42,00,000
Add:		
(i) Cultivation expenses	4,00,000	
(ii) Expenses of I.U. located in Free Trade Zone (Sec. 10A)	1,50,000	
(iii) Expenses of I.U. under Sec. 10B	1,00,000	
(iv) Provision of loss of subsidiary	4,00,000	
(v) Provision for bad and doubtful debts— an unascertained liability	2,00,000	
(vi) Provision for bills under discount— an unascertained liability	50,000	
(vii) Provision for wealth-tax, sales- tax, against demand notice— an ascertained liability	—	
(viii) Income-tax provision— an ascertained liability to be added back	3,00,000	
(ix) Dividend paid on preference shares	2,00,000	
(x) Proposed dividend on equity shares	4,00,000	
(xi) Transfer to general reserve	1,00,000	
(xii) Dividend Equalisation reserve	2,00,000	
(xiii) Depreciation [Sec. 115JB(2)(g) w.e.f. AY 2011-2012]	<u>3,00,000</u>	<u>28,00,000</u>
Adjusted profits		70,00,000
Less:		
(i) Sales of agriculture produce [Sec. 10(1)]	10,00,000	
(ii) Receipt from I.U. in Free Trade Zone [Sec. 10A]	2,00,000	
(iii) Receipt from I.U. Sec. 10B	2,00,000	
(iv) Depreciation, excluding depreciation on account of revaluation of assets	2,00,000	
(v) Brought forward loss or depreciation, whichever is less.	9,00,000	
(vi) Withdrawals from Reserve & Provision for free sale service, under warranty scheme	9,50,000	
(vii) Long-term capital gain on transfer of equity shares [Sec. 10(38)] — see Note below	Nil	
(viii) Receipts from UTI [Sec. 10(35)]	<u>50,000</u>	<u>35,00,000</u>
Book-profits		35,00,000

Note: 1. Calculation of brought forward losses or depreciation:

2007-2008	Loss	5,00,000
2008-2009	Loss/depreciation	Nil
2009-2010	Depreciation	4,00,000
2010-2011	Loss/depreciation	Nil

1. Transfer from provision for after sale service, free of cost, made during the year 2005-2006, debited to profit and loss a/c and now credited to profit and loss a/c and now credited to profit and loss a/c is an allowable deduction [Sec. 115-JB(2)].
2. Long-term capital gain from the transfer of equity shares in a company is exempt is chargeable to securities trans action tax (STT). However, for the purposes of computing book-profits, it is not to be deducted [Sec. 10(38)]. Accordingly, the expenditure incurred for the transfer of equity shares has not been added back in computing book profits.

Illustration 3. Classic Exporters Ltd, runs a new industrial undertaking set up in 2006-2007 which satisfies the conditions of Sec. 80-IB. Given below is the profit and loss account for the previous year 2011-2012 :

Particulars	₹	Particulars	₹
Stock	4,00,000	Domestic sales	24,00,000
Purchases	23,00,000	Export sales	43,00,000
Salaries and wages	9,70,000	Export incentives Sec. 28(iia)/(iic)	50,000
Entertainment expenses	1,30,000	Profit of foreign branch	2,50,000
Freights and insurance attributable to exports	3,00,000	Brokerage/commission/interest/rent, etc	50,000
Travelling expenses	2,20,000	Transfer from contingency reserve	10,00,000
Depreciation	1,50,000	Stock	3,50,000
Selling expenses	1,20,000		
Income tax paid	90,000		
Income-tax penalty	20,000		
Wealth tax paid	10,000		
Custom duty payable against demand notice	30,000		
Provision for unascertained liabilities	20,000		
Provision for ascertained liabilities	50,000		
Proposed dividend	3,00,000		
Loss of subsidiary company	50,000		
Net profit	32,40,000		
	84,00,000		84,00,000

You are further informed:

- (i) Excise duty for 2010-2011, amounting ₹ 1,20,000 was paid on 15 December 2011.
- (ii) Depreciation under Sec. 32 is ₹ 2,20,000.
- (iii) During the year 2008-2009, contingency reserve, amounting ₹ 10,00,000, debited to profit and loss a/c, was added back to the extent of ₹ 4,00,000 in the computation of book-profits. The company has transferred the said reserve to the profit and loss a/c during the year.
- (iv) Brought forward business loss/depreciation:

PY	Accounting purposes		Tax purposes	
	Loss	Depreciation	Loss	Depreciation
2007-2008	(-) 10,00,000	(-) 1,00,000	(-) 5,00,000	(-) 2,50,000
2008-2009	(-) 2,00,000	(-) 3,00,000	(-) 1,00,000	(-) 2,00,000

Compute the following: (a) Total income, (b) Book-profits and (c) Tax liability.

Computation of total income for the AY 2012-2013

Particulars	₹	₹
Net profit as per Profit & Loss A/c		32,40,000
Add : <u>Expenses debited to P/L A/c – disallowed</u>		
(i) Income tax	90,000	
(ii) Wealth tax	10,000	
(iii) Custom duty payable	30,000	
(iv) Provision for unascertained liability	20,000	
(v) Proposed dividend	3,00,000	
(vi) Loss of subsidiary company	50,000	
(vii) Income-tax penalty	20,000	5,20,000
		<u>37,60,000</u>
Less : <u>Allowable Expenses and wrong credits in P/L A/c</u>		
(i) Withdrawals from contingency reserve	10,00,000	
(ii) Excise duty	1,20,000	
(iii) Depreciation	70,000	
(iv) Brokerage, commission, interest and rent, etc.	50,000	12,40,000
		<u>25,20,000</u>
Business profits		25,20,000
Add: Income from other sources: Brokerage/ commission, etc.		50,000
		<u>25,70,000</u>
Aggregate income		25,70,000
Less: (i) Brought forward losses (Sec. 72)	6,00,000	
(ii) Brought forward depreciation [Sec. 32(2)]	4,50,000	10,50,000
		<u>15,20,000</u>
Gross Total Income		15,20,000
Less: Profit from industrial undertaking Sec. 80IB: 30% of ₹ 15,20,000 as included in GTI		4,56,000
		<u>10,64,000</u>
Total Income		10,64,000


(b) Computation of Book Profits for the AY 2012-2013

Particulars	₹	₹
Net profits as per Profit & Loss A/c		32,40,000
Add : <u>Expenses disallowed</u>		
(i) Income tax	90,000	
(ii) Provision for unascertained liability	20,000	
(iii) Proposed dividend	3,00,000	
(iv) Loss of subsidiary	50,000	4,60,000
		37,00,000
Less : <u>Allowable expenses and wrong credit in P/L A/c</u>		
(i) Withdrawals from contingency reserve	4,00,000	
(ii) Brought forward business loss or depreciation whichever is less		
2007-2008 Depreciation	1,00,000	
2008-2009 Loss	2,00,000	7,00,000
Book-profits		30,00,000

(c) Computation of tax liability for the AY 2012-2013

Particulars	₹
(a) Tax on Total Income (including Education Cess and SHEC) = 30.9% of 10,64,000	3,28,776
(b) Tax on Book Profits (including Education Cess and SHEC) = 19.055% on 30,00,000	5,71,650
Tax payable	5,71,650

Note :

- No adjustment is required for depreciation debited to profit and loss a/c because it is not on account of revaluation of any asset.
- MAT credit available ₹ (5,71,650 – 3,28,776) = ₹ 2,42,874

Illustration 4. Z Ltd is a qualifying shipping company which has got two qualifying ships during the previous year 2011-2012 :

Ship	Tonnage weight	No. of operational days
Ship A	37,949 tonnes and 990 kg	300 days
Ship B	25,550 tonnes and 275 kg	365 days

Compute its tonnage income under Tonnage Tax Scheme for the assessment year 2012-2013.

Solution:

Ship A	Ship B
(i) Tonnage consisting of kilograms is ignored. (ii) If such tonnage is not a multiple of 100 tonnes and the last two digits are less than 50, the tonnage is reduced to the previous lower tonnage which is a multiple of 100. (iii) Tonnage rounded off = 37,900 tonnes	(i) Tonnage consisting of kilograms is ignored. (ii) If such tonnage is not a multiple of 100, and last two digits are 50 or more, the tonnage is increased to next higher tonnage which is a multiple of 100 (iii) Tonnage rounded off - 25,600 tonnes

Income— computation under TTS		Income— computation under TTS	
Daily TI:	₹	Daily TI:	₹
First 1,000 tonnes = ₹ 46 × 10 =	460	First 1,000 tonnes = ₹ 46 × 10 =	460
Next 9,000 tonnes = ₹ 35 × 90 =	3150	Next 9,000 tonnes = ₹ 35 × 90 =	3150
Next 15,000 tonnes = ₹ 28 × 150 =	4200	Next 15,000 tonnes = ₹ 28 × 150 =	4200
Balance 12,900 tonnes = ₹ 19 × 129 =	2451	Balance 600 tonnes = ₹ 19 × 6 =	114
Daily TI:	10,261	Daily TI:	7,924
Total TI for the previous year ₹ 10,261 × 300 =	30,78,300	Total TI for the previous year ₹ 7,924 × 365	28,92,260



STUDY NOTE - 18

GRIEVANCES REDRESSAL PROCEDURE

This Study Note includes

- Provisions relating to Grievances Redressal Procedure

GRIEVANCES REDRESSAL PROCEDURE

When the assessment order is passed against the assessee, and if he is not satisfied with any order passed by the assessing officer, he may appeal to higher court. Procedure for appeal is laid down under the act.

The redressal procedure under the act includes the following:

1. Rectification
2. Appeal
3. Revision

18.1 RECTIFICATION

Sec. 154 : Rectification of mistake.

- (1) With a view to rectifying any mistake apparent from the record an income-tax authority referred to in section 116 may, —
 - (a) amend any order passed by it under the provisions of this Act;
 - (b) amend any intimation or deemed intimation under sub-section (1) of section 143.
- (1A) Where any matter has been considered and decided in any proceeding by way of appeal or revision relating to an order referred to in sub-section (1), the authority passing such order may, notwithstanding anything contained in any law for the time being in force, amend the order under that sub-section in relation to any matter other than the matter which has been so considered and decided.
- (2) Subject to the other provisions of this section, the authority concerned-
 - (a) may make an amendment under sub-section (1) of its own motion, and
 - (b) shall make such amendment for rectifying any such mistake which has been brought to its notice by the assessee, and where the authority concerned is the Commissioner (Appeals), by the Assessing Officer also.
- (3) An amendment, which has the effect of enhancing an assessment or reducing a refund or otherwise increasing the liability of the assessee, shall not be made under this section unless the authority concerned has given notice to the assessee of its intention so to do and has allowed the assessee a reasonable opportunity of being heard.

At whose instance mistakes can be rectified :

- The concerned authority may [implies discretion] make the necessary amendment of its own motion.

- The concerned authority has to make [implies that there is no discretion] such amendment for rectifying any mistake brought to its notice by the assessee.
- Where the concerned authority is the Commissioner (Appeals) and the mistake has been brought to his notice by the Assessing Officer, it has to make such amendment [implies that there is no discretion].

Procedure for such rectification under sub-section (3) and (5),

- An amendment of the following nature can be made only after the concerned authority has given notice in this respect and also a reasonable opportunity of being heard to the assessee
 - (a) Amendment which enhances an assessment.
 - (b) Amendment which reduces a refund.
 - (c) Amendment which otherwise increases the liability of the assessee.
- If any amendment enhances the assessment or reduces a refund already made, a notice of demand is served on the assessee. Such notice is deemed to be a notice u/s 156.
- If any amendment reduces the assessment, refund due to the assessee is made unless it is withheld u/s 241.

Time Limit for Rectification:

Period of limitation for making rectification as prescribed in sub-section (7) is as follows:

- No amendment under this section can be made after the expiry of 4 years from the end of the financial year in which the order sought to be amended was passed. It may be noted that an amendment is made when the related order is passed.
- This period of limitation is not applicable in case the provision of section 155 are applicable.
- However, if a valid application has been made by the assessee for rectification within the statutory time limit but is not disposed of by the concerned authority within the time specified, it may be disposed of even after the expiry of such time limit [Circular No. 73, dated 7th January, 1972]. This relief is, however, not admissible in case rectification proceedings are initiated by the department itself.

Action against rectification order:

Following action may be taken against a rectification order :

- Appeal can be made to the Commissioner (Appeals) u/s 246A. Appeal can also be made against an order passed under this section refusing to rectify a mistake {Chennai Prop. & Inv. Ltd. v. CIT [2001] 247 ITR 226 (Mad.)}.
- Appeal can be made to the Appellate Tribunal u/s 253.
- Revision application can be made u/s 264.

Sec. 155 : Other amendments.

- (1) Where, in respect of any completed assessment of a partner in a firm for the assessment year commencing on the 1st day of April, 1992, or any earlier assessment year, it is found-
 - (a) on the assessment or reassessment of the firm, or
 - (b) on any reduction or enhancement made in the income of the firm under this section, section 154, section 250, section 254, section 260, section 262, section 263 or section 264, or
 - (c) on any order passed under sub-section (4) of section 245D on the application made by the firm, that the share of the partner in the income of the firm has not been included in the assessment of the partner or, if included, is not correct, the Assessing Officer may amend the order of assessment of the



partner with a view to the inclusion of the share in the assessment or the correction thereof, as the case may be; and the provisions of section 154 shall, so far as may be, apply thereto, the period of four years specified in sub-section (7) of that section being reckoned from the end of the financial year in which the final order was passed in the case of the firm.

- (2) Where as a result of proceedings initiated under section 147, a loss or depreciation has been recomputed and in consequence thereof it is necessary to recompute the total income of the assessee for the succeeding year or years to which the loss or depreciation allowance has been carried forward and set off under the provisions of sub-section (1) of section 72, or sub-section (2) of section 73, or sub-section (1) or sub-section (3) of section 74, or sub-section (3) of section 74A, the Assessing Officer may proceed to recompute the total income in respect of such year or years and make the necessary amendment; and the provisions of section 154 shall, so far as may be, apply thereto, the period of four years specified in sub-section (7) of that section being reckoned from the end of the financial year in which the order was passed under section 147.
- (3) Where any deduction in respect of any expenditure on scientific research has been made in any assessment year under sub-section (2B) of section 35 and the assessee fails to furnish a certificate of completion of the programme obtained from the prescribed authority within one year of the period allowed for its completion by such authority, the deduction originally made in excess of the expenditure actually incurred shall be deemed to have been wrongly made, and the Assessing Officer may, notwithstanding anything contained in this Act, recompute the total income of the assessee for the relevant previous year and make the necessary amendment; and the provisions of section 154 shall, so far as may be, apply thereto, the period of four years specified in sub-section (7) of that section being reckoned from the end of the previous year in which the period allowed for the completion of the programme by the prescribed authority expired.
- (4) Where as a result of any proceeding under this Act, in assessment for any year of a company is whose case an order under section 104 has been made for that year, it is necessary to recompute the distributable income of that company, the Assessing Officer may proceed to recompute the distributable income and determine the tax payable on the basis of such recomputation and make the necessary amendment; and the provisions of section 154 shall, so far as may be, apply thereto, the period of four years specified in sub-section (7) of that section being reckoned from the end of the financial year in which the final order was passed in the case of the company in respect of that proceeding.
- (5) Where in the assessment for any year, a capital gain arising from the transfer of a long-term capital asset, is charged to tax and within a period of six months after the date of such transfer, the assessee has made any investment or deposit in any specified asset within the meaning of Explanation 1 to sub-section (1) of section 54E, the Assessing Officer shall amend the order of assessment so as to exclude the amount of the capital gain not chargeable to tax under the provisions of sub-section (1) of section 54E; and the provisions of section 154 shall, so far as may be, apply thereto, the period of four years specified in sub-section (7) of that section being reckoned from the end of the financial year in which the assessment was made.
- (6) Where in the assessment for any year, a capital gain arising from the transfer of any original asset as is referred to in section 54H is charged to tax and within the period extended under that section the assessee acquires the new asset referred to in that section or, as the case may be, deposits or invests the amount of such capital gain within the period so extended, the Assessing Officer shall amend the order of assessment so as to exclude the amount of the capital gain not chargeable to tax under any of the sections referred to in section 54H; and the provisions of section 154 shall, so far as may be, apply thereto, the period of four years specified in sub-section (7) of section 154 being reckoned from the end of the previous year in which the compensation was received by the assessee.
- (7) Where in the assessment for any year commencing before the 1st day of April, 1988, the deduction under section 80-O in respect of any income, being the whole or any part of income by way of royalty, commission, fees or any similar payment as is referred to in that section, has not been allowed on the ground that such income has not been received in convertible foreign exchange in India, or having

been received in convertible foreign exchange outside India, or having been converted into convertible foreign exchange outside India, has not been brought into India, by or on behalf of the assessee in accordance with any law for the time being in force for regulating payments and dealings in foreign exchange and subsequently such income or part thereof has been or is received in, or brought into, India in the manner aforesaid, the Assessing Officer shall amend the order of assessment so as to allow deduction under section 80-O in respect of such income or part thereof as is so received in, or brought into, India; and the provisions of section 154 shall, so far as may be, apply thereto, the period of four years specified in sub-section (7) of that section being reckoned from the end of the previous year in which such income is so received in, or brought into, India; so, however, that the period from the 1st day of April, 1988 to the 30th day of September, 1991 shall be excluded in computing the period of four years.

- (8) Where in the assessment for any year, the deduction under section 80HBB or section 80HBC or section 80HBD or section 80HBE or section 80-O or section 80R or section 80RR or section 80RRA has not been allowed on the ground that such income has not been received in convertible foreign exchange in India, or having been received in convertible foreign exchange outside India, or having been converted into convertible foreign exchange outside India, has not been brought into India, by or on behalf of the assessee with the approval of the Reserve Bank of India or such other authority as is authorised under any law for the time being in force for regulating payments and dealings in foreign exchange and subsequently such income or part thereof has been or is received in, or brought into, India in the manner aforesaid, the Assessing Officer shall amend the order of assessment so as to allow deduction under section 80HBB or section 80HBC or section 80HBD or section 80HBE or section 80-O or section 80R or section 80RR or section 80RRA, as the case may be, in respect of such income or part thereof as is so received in, or brought into, India; and the provisions of section 154 shall, so far as may be, apply thereto, and the period of four years shall be reckoned from the end of the previous year in which such income is so received in, or brought into India.
- (9) Where in the assessment for any year, a capital gain arising from the transfer of a capital asset, being land or building or both, is computed by taking the full value of the consideration received or accruing as a result of the transfer to be the value adopted or assessed by any authority of a State Government for the purpose of payment of stamp duty in accordance with sub-section (1) of section 50C, and subsequently such value is revised in any appeal or revision or reference referred to in clause (b) of sub-section (2) of that section, the Assessing Officer shall amend the order of assessment so as to compute the capital gain by taking the full value of the consideration to be the value as so revised in such appeal or revision or reference; and the provisions of section 154 shall, so far as may be, apply thereto, and the period of four years shall be reckoned from the end of the previous year in which the order revising the value was passed in that appeal or revision or reference.

18.2 APPEAL AND APPELLATE HIERARCHY

Appeal is a complaint to a higher court relating to an injustice done by a lower court. The party complaining is called “appellant” and the other party is known as “respondent”. There are various provisions in the Income-tax Act relating to appeals and revision of orders.

Under the Income-tax Act, the following remedial measures are available to the assessee if he is not satisfied with any order passed by the assessing officer :-

- (i) **Appeal** W.e.f. 1.10.1998 first shall lie with the Commissioner of Income Tax (Appeals) against the order of the assessing officer (sec. 246A), or
- (ii) **Revision** if appeal is not preferred or it could not be filed within the time limit allowed, the assessee can apply u/s. 264 to the Commissioner of Income Tax for revision of orders passed by the assessing officer.

The Commissioner of Income-tax can also take up suo moto the case for revision. Where, however, in the opinion of the Commissioner of Income Tax the order passed by the assessing officer is erroneous and prejudicial to the interest of revenue, the Commissioner of Income Tax can also take up the case for revision u/s. 263.

**Appeal to Commissioner of Income Tax (Appeals) [Sec. 246A]**

An aggrieved assessee may appeal to the Commissioner of Income Tax (Appeals) against the following orders of Assessing officer-

- a) an order against the assessee, where the assessee denies his liability to be assessed under this Act; or
- b) any order of assessment u/s. 143(3) or 144, where the assessee objects :
 - to the income assessed, or
 - to the amount of tax determined, or
 - to the amount of loss computed, or
 - to the status under which he is assessed;
- c) an order of assessment, reassessment or recomputations u/s. 147 or sec. 150;
- d) an order or rectification made u/s. 154 or order u/s. 155 having the effect of :
 - enhancing the assessment, or
 - reducing a refund, or
 - order refusing to allow the claim made by the assessee under either of these sections;
- e) an order u/s. 163 treating the assessee as the agent of a non-resident;
- f) an order u/s. 170(2), (3) relating to succession to business otherwise than on death;
- g) an order u/s. 171 relating to assessment after partition of a HUF;
- h) an order u/s. 201 treating the assessee deemed to be assessee in default for failure to deduct the whole or any part of the tax or pay tax after deduction ;
- i) an order u/s. 237 relating to refunds;
- j) an order imposing penalty u/ss. 221, 271, 271A, 271B, 271F and 272BB;
- k) an order made by Joint Commissioner imposing a penalty u/ss. 271C, 271D, 271E and 272AA;
 - l) an order of Joint Commissioner/Joint Director imposing a penalty u/s. 272A;
- m) an order imposing a penalty under chapter XXI i.e. u/ss. 270 to 275;
- n) an order of assessment made by an Assessing officer under clause (c) of section 158BC i.e. Block Assessment, in respect of search initiated u/s. 132 or books of account, other documents or any asset requisitioned u/s. 132A, on or after 1.1.1997;
- o) an order imposing a penalty u/s. 158BFA(2) in case of Block Assessment ;
- p) an order made by an Assessing officer other than Deputy/Joint Commissioner under the provisions of this Act in the case of such person or class of persons, as the Board may, having regard to the nature of the cases, the complexities involved and other relevant considerations direct.

Case Laws:

1. Non-allowing of interest in rectification order is appealable: When the ITO rectifies an assessment under section 154/155 and grants refund but fails to grant interest on the refund, such rectificatory order has the effect of reducing the amount payable to the assessee and hence appealable under section 246(1)(b) - *CIT v. Perfect Pottery Co. Ltd.* 173 ITR 545

2. Denial of liability to tax under particular circumstances is also covered - The expression 'denial of liability' is comprehensive enough to take in not only the total denial of liability but also the liability to tax under particular circumstances. Thus, an assessee has a right of appeal against the order of the ITO assessing the AOP instead of the members thereof individually - *CIT v. Kanpur Coal Syndicate* 53 ITR 225
3. Objection as to place of assessment cannot be raised - No appeal can lie against an order determining the place of assessment - *Rai Bahadur Seth Teomal v. CIT* 36 ITR 9

Amendment in section 246A(1) regarding appeal to Commissioner (Appeals) [Section 246A(1)] (W.e.f. 1-10-2009)

The Act has amended section 246A(1)(o) to provide that the appeal against the order passed by the Assessing Officer under section 143(3) or order of re-assessment under section 147 except an order passed in pursuance of directions of Dispute Resolution Panel shall lie to the Commissioner (Appeals).

Appeal by person denying liability to deduct tax in certain cases.[Sec. 248]

Where under an agreement or other arrangement, the tax deductible on any income, other than interest, under section 195 is to be borne by the person by whom the income is payable, and such person having paid such tax to the credit of the Central Government, claims that no tax was required to be deducted on such income, he may appeal to the Commissioner (Appeals) for a declaration that no tax was deductible on such income.

Case Law:

1) AAC can determine quantum also : In an appeal filed under section 248, AAC has jurisdiction to deal with the quantum of sum chargeable under the provisions of the Act on which the assessee is liable to deduct tax under section 195 - *CIT v. Westman Engg. Co. (P.) Ltd.* 188 ITR 327

Procedure for filing appeal [Sec. 249 & Rules 45 & 46]

- (i) An appeal in Form No. 35 should be filed within 30 days of -
 - a) the date of service of notice of demand relating to assessment or penalty if it relates to assessment or penalty; or
 - b) the date of payment of tax, if it relates to any tax deducted u/s. 195(1) in respect of payment to non-resident in certain cases; or
 - c) the date on which intimation of the order sought to be appealed against is served if it relates to any other cases.

The Commissioner of Income-tax (Appeals) may condone the delay in filing appeal petition if he satisfied that the appellant had sufficient cause for not presenting it within that period.

- (ii) No appeal shall be admitted unless at the time of filing of appeal the appellant has paid :-
 - (a) the tax due on the income returned by him, or
 - (b) where no return has been filed the assessee has paid the amount equal to the amount of advance tax which was payable by him. However, the Commissioner (Appeals) may, for any good and sufficient reason to be recorded in writing, exempt the appellant from the payment of such tax.
- (iii) Appeal is required to be made in duplicate. The memorandum of appeal, statement of facts and grounds of appeal should be accompanied by a copy of the order appealed against and the notice of demand in original, if any.
- (iv) **Fee for filing appeal :** The memorandum of appeal shall be accompanied by a fee as under :-

a) Where assessed income is ₹ 1,00,000 or less	₹ 250
b) Where assessed income exceeds ₹ 1,00,000 but does not exceed ₹ 2,00,000	₹ 500
c) Where assessed income exceeds ₹ 2,00,000	₹ 1,000



W.e.f. 1.6.1999 fee for filing appeal relating to matters which may not have nexus with the returned income (e.g. TDS defaults, non-filing of return) has been prescribed to be ₹250 for appeal before Commissioner (Appeals). [Sec. 249]

The Commissioner (Appeals) after hearing the assessee and the income-tax department will pass an order in writing and communicate his order to the Assessee and the Commissioner of Income Tax. The Commissioner (Appeals) may confirm, reduce, enhance or annul an assessment against which the appeal is made. However, he has no power to set aside the assessment and refer the case back to the assessing officer for making a fresh assessment according to his direction. He may confirm or cancel the order of penalty. In other cases, he can pass such orders as he thinks fit. [Sec. 251]

Case Laws:

- (1) Demand notice need not be enclosed to memo of appeal - Neither section 249 nor rule 45 makes it incumbent on the assessee-appellant to enclose the demand notice along with the memo of appeal - *Addl. CIT v. Prem Kumar Rastogi* 115 ITR 503
- (2) Appellate authority is statutorily bound to consider condonation of delay - Where an application for condonation of delay in filing an appeal is preferred, it is the statutory obligation of the appellate authority to consider whether sufficient cause for not presenting the appeal in time was shown by the appellant - *Shrimant Govindrao Narayanrao Ghorpade v. CIT* 48 ITR 54

Procedure in appeal.[Sec. 250]

- (1) The [Commissioner (Appeals)] shall fix a day and place for the hearing of the appeal, and shall give notice of the same to the appellant and to the [Assessing] Officer against whose order the appeal is preferred.
- (2) The following shall have the right to be heard at the hearing of the appeal—
 - (a) the appellant, either in person or by an authorised representative;
 - (b) the [Assessing] Officer, either in person or by a representative.
- (3) The [Commissioner (Appeals)] shall have the power to adjourn the hearing of the appeal from time to time.
- (4) The [Commissioner (Appeals)] may, before disposing of any appeal, make such further inquiry as he thinks fit, or may direct the [Assessing] Officer to make further inquiry and report the result of the same to the [Commissioner (Appeals)].
- (5) The [Commissioner (Appeals)] may, at the hearing of an appeal, allow the appellant to go into any ground of appeal not specified in the grounds of appeal, if the [Commissioner (Appeals)] is satisfied that the omission of that ground from the form of appeal was not wilful or unreasonable.
- (6) The order of the [Commissioner (Appeals)] disposing of the appeal shall be in writing and shall state the points for determination, the decision thereon and the reason for the decision.
- [(6A) In every appeal, the Commissioner (Appeals), where it is possible, may hear and decide such appeal within a period of one year from the end of the financial year in which such appeal is filed before him under sub-section (1) of section 246A.]
- (7) On the disposal of the appeal, the [Commissioner (Appeals)] shall communicate the order passed by him to the assessee and to the [Chief Commissioner or Commissioner].

Case Laws:

- 1) Appeal once filed cannot be withdrawn - An assessee having once filed an appeal, cannot withdraw it. Even if the assessee refuses to appear at the hearing, the AAC can proceed with the enquiry and if he finds that there has been an under-assessment, he can enhance the assessment - *CIT v. Rai Bahadur Hardutroy Motilal Chamaria* 66 ITR 443 (SC)/*CIT v. B.N. Bhattachargee* 118 ITR 461

- 2) Revenue can object to delay in filing appeal - If an appeal by an assessee is admitted without the fact of delay in its presentation having been noticed, it is open to the department to raise the objection at the time of hearing of the appeal - *Mela Ram & Sons v. CIT* 29 ITR 607

Powers of the [Commissioner (Appeals)] [Sec. 251]

(1) In disposing of an appeal, the [Commissioner (Appeals)] shall have the following powers—

- (a) in an appeal against an order of assessment, he may confirm, reduce, enhance or annul the assessment
- (b) in an appeal against an order imposing a penalty, he may confirm or cancel such order or vary it so as either to enhance or to reduce the penalty;
- (c) in any other case, he may pass such orders in the appeal as he thinks fit.

(2) The [Commissioner (Appeals)] shall not enhance an assessment or a penalty or reduce the amount of refund unless the appellant has had a reasonable opportunity of showing cause against such enhancement or reduction.

Explanation.—In disposing of an appeal, the [Commissioner (Appeals)] may consider and decide any matter arising out of the proceedings in which the order appealed against was passed, notwithstanding that such matter was not raised before the [Commissioner (Appeals)] by the appellant.

Appellate Tribunal. [Sec. 252]

- (1) The Central Government shall constitute an Appellate Tribunal consisting of as many judicial and accountant members as it thinks fit to exercise the powers and discharge the functions conferred on the Appellate Tribunal by this Act.
- (2) A judicial member shall be a person who has for at least ten years held a judicial office in the territory of India or who has been a member of the [Indian] Legal Service and has held a post in Grade [II] of that Service or any equivalent or higher post for at least three years or who has been an advocate for at least ten years.

Explanation.—For the purposes of this sub-section,—

- (i) in computing the period during which a person has held judicial office in the territory of India, there shall be included any period, after he has held any judicial office, during which the person has been an advocate or has held the office of a member of a Tribunal or any post, under the Union or a State, requiring special knowledge of law;
- (ii) in computing the period during which a person has been an advocate, there shall be included any period during which the person has held judicial office or the office of a member of a Tribunal or any post, under the Union or a State, requiring special knowledge of law after he became an advocate.
- (2A) An accountant member shall be a person who has for at least ten years been in the practice of accountancy as a chartered accountant under the Chartered Accountants Act, 1949 (38 of 1949), or as a registered accountant under any law formerly in force or partly as a registered accountant and partly as a chartered accountant, or who has been a member of the Indian Income-tax Service, Group A and has held the post of [Additional] Commissioner of Income-tax or any equivalent or higher post for at least three years.]
- (3) The Central Government shall appoint the Senior Vice-President or one of the Vice-Presidents of the Appellate Tribunal to be the President thereof.]
- (4) The Central Government may appoint one or more members of the Appellate Tribunal to be the Vice-President or, as the case may be, Vice-Presidents thereof.]
- [(4A) The Central Government may appoint one of the Vice-Presidents of the Appellate Tribunal to be the Senior Vice-President thereof.]
- (5) [The Senior Vice-President or a Vice-President] shall exercise such of the powers and perform such of the functions of the President as may be delegated to him by the President by a general or special order in writing.



Appeal to the Appellate Tribunal [Sec. 253]

The Appellate Tribunal is constituted by the Central Government and has two classes of members – judicial and accountant.

An assessee may file an appeal before the Appellate Tribunal against the following orders u/s. 253(1) :-

- (a) an order passed by Commissioner (Appeals), in the following cases :
 - (i) an order u/s. 250 i.e. order passed on the appeal filed before him.
 - (ii) an order imposing penalty u/s. 271, 271A, 272A.
 - (iii) an order u/s. 154 regarding rectification of mistakes in an order passed, if the rectification has not been satisfactorily done by him.
- (b) (i) an order passed by a Commissioner u/s. 12AA relating to registration of a trust or institution ;
 - (ii) an order passed by a Commissioner u/s. 263 or u/s. 272A; or
 - (iii) order passed by a Chief Commissioner, Director General or Director u/s. 272A imposing penalty; or
 - (iv) order passed u/s. 154 amending his order u/s. 263.

The Commissioner may also, if he objects to any order passed by the Commissioner (Appeals) u/s. 154/250, direct the assessing officer to appeal to the Appellate Tribunal against the order [Sec. 253(2)].

It may be mentioned that the Appellate Tribunal is the fact finding authority and hence the order passed by it on questions of fact are final and conclusive.

The appeal should be filed in Form 36, in triplicate, accompanied by :

1. Two copies (at least one of which should be certified copy) of the order appealed against and two copies of the relevant order of the Assessing officer.
2. Challan as proof of payment of appeal fee. The fee is payable as follows :

(a) Total income assessed is upto ₹ 1,00,000	Fee of ₹ 500
(b) Total Income assessed is ₹ 1,00,001 to ₹2,00,000	Fee of ₹ 1500
(c) Total Income assessed is over ₹ 2,00,000 assessed subject to a maximum of ₹10,000	Fee of 1% of the income
(d) Where the subject-matter of appeal is not covered under (a), (b), (c) above	Fee of ₹ 500
(e) Application for stay of demand	Fee of ₹ 500

3. Three copies of the paper book containing copies of all documents, if any, to be relied upon.
4. Three copies of any order of the Tribunal or a High Court or the Supreme Court, relied upon.

Where the department prefers an appeal against the order of Commissioner (Appeals) to the Appellate Tribunal a notice of the same along with a copy of the appeal shall be served on the assessee. The assessee should furnish a memorandum of cross objections in Form No. 36A before the Appellate Tribunal within 30 days of receipt of such notice. Similarly, the department can also file a cross objections before the tribunal on an assessee's appeal.

The tribunal may decide the appeal within four years from the end of the Financial Year in which such appeal is filed. Where the tribunal has issued a stay order, the appeal shall be disposed of within a period of 180 days from the date of stay order otherwise the stay order shall stand vacated (on expiry of the said period). [Sec. 254(2A)]

Case Law:

i) Where Tribunal found that cross-objections were belated by a period of one year and eleven months and Tribunal came to conclusion that no sufficient cause had been made out explaining delay, Tribunal was justified in holding that delay in filing cross-objections could not be condoned - *Vareli Textile Industries v. CIT* 154 Taxman 33.

Amendment in section 253(1) regarding appeals to ITAT [Section 253(1) | (W.e.f. 1-10-2009)]

The Act has inserted clause (d) to section 253(1) to provide that appeal against the order passed under section 143(3) or order of re-assessment under section 147 by the Assessing Officer in pursuance of directions of the Dispute Resolution Panel or an order passed under section 154 in respect of such order shall lie to the ITAT directly.

Orders of Appellate Tribunal [Sec. 254]

(1) The Appellate Tribunal may, after giving both the parties to the appeal an opportunity of being heard, pass such orders thereon as it thinks fit.

(2) The Appellate Tribunal may, at any time within four years from the date of the order, with a view to rectifying any mistake apparent from the record, amend any order passed by it under sub-section (1), and shall make such amendment if the mistake is brought to its notice by the assessee or the [Assessing] Officer :

Provided that an amendment which has the effect of enhancing an assessment or reducing a refund or otherwise increasing the liability of the assessee, shall not be made under this sub-section unless the Appellate Tribunal has given notice to the assessee of its intention to do so and has allowed the assessee a reasonable opportunity of being heard :

Provided that the Appellate Tribunal may, after considering the merits of the application made by the assessee, pass an order of stay in any proceedings relating to an appeal filed under sub-section (1) of section 253, for a period not exceeding one hundred and eighty days from the date of such order and the Appellate Tribunal shall dispose of the appeal within the said period of stay specified in that order:

Provided further that where such appeal is not so disposed of within the said period of stay as specified in the order of stay, the Appellate Tribunal may, on an application made in this behalf by the assessee and on being satisfied that the delay in disposing of the appeal is not attributable to the assessee, extend the period of stay, or pass an order of stay for a further period or periods as it thinks fit; so, however, that the aggregate of the period originally allowed and the period or periods so extended or allowed shall not, in any case, exceed three hundred and sixty-five days and the Appellate Tribunal shall dispose of the appeal within the period or periods of stay so extended or allowed:

Provided also that if such appeal is not so disposed of within the period allowed under the first proviso or the period or periods extended or allowed under the second proviso, the order of stay shall stand vacated after the expiry of such period or periods.

(2B) The cost of any appeal to the Appellate Tribunal shall be at the discretion of that Tribunal.]

(3) The Appellate Tribunal shall send a copy of any orders passed under this section to the assessee and to the [Commissioner].

(4) [Save as provided in the National Tax Tribunal Act, 2005], orders passed by the Appellate Tribunal on appeal shall be final.

Case Laws:

1. *Jurisdiction is not higher than that of ITO* – The jurisdiction of the Tribunal in the hierarchy created by the Act is no higher than that of the ITO; it is also confined to the year of assessment *ITO v. Murlidhar Bhagwan Das* 52 ITR 335.

2. *Tribunal cannot assume powers inconsistent with statutory provisions* – *CIT v. Manick Sons* 74 ITR

3. *Jurisdiction is restricted to subject-matter of appeal*- The powers of the Tribunal in dealing with appeals are expressed in section 254(1) in the widest possible terms. The word ‘thereon’ of course restricts the jurisdiction of the Tribunal to the subject-matter of the appeal *Hukumchand Mills Ltd. v. CIT* 63 ITR 232 .



Procedure of Appellate Tribunal [Sec. 255]

- (1) The powers and functions of the Appellate Tribunal may be exercised and discharged by Benches constituted by the President of the Appellate Tribunal from among the members thereof.
- (2) Subject to the provisions contained in sub-section (3), a Bench shall consist of one judicial member and one accountant member.
- (3) The President or any other member of the Appellate Tribunal authorised in this behalf by the Central Government may, sitting singly, dispose of any case which has been allotted to the Bench of which he is a member and which pertains to an assessee whose total income as computed by the [Assessing] Officer in the case does not exceed [five hundred thousand rupees], and the President may, for the disposal of any particular case, constitute a Special Bench consisting of three or more members, one of whom shall necessarily be a judicial member and one an accountant member.
- (4) If the members of a Bench differ in opinion on any point, the point shall be decided according to the opinion of the majority, if there is a majority, but if the members are equally divided, they shall state the point or points on which they differ, and the case shall be referred by the President of the Appellate Tribunal for hearing on such point or points by one or more of the other members of the Appellate Tribunal, and such point or points shall be decided according to the opinion of the majority of the members of the Appellate Tribunal who have heard the case, including those who first heard it.
- (5) Subject to the provisions of this Act, the Appellate Tribunal shall have power to regulate its own procedure and the procedure of Benches thereof in all matters arising out of the exercise of its powers or of the discharge of its functions, including the places at which the Benches shall hold their sittings.
- (6) The Appellate Tribunal shall, for the purpose of discharging its functions, have all the powers which are vested in the income-tax authorities referred to in section 131, and any proceeding before the Appellate Tribunal shall be deemed to be a judicial proceeding within the meaning of sections 193 and 228 and for the purpose of section 196 of the Indian Penal Code (45 of 1860), and the Appellate Tribunal shall be deemed to be a civil court for all the purposes of section 195 and Chapter XXXV of the Code of Criminal Procedure, 1898 (5 of 1898).

Case Laws :

1. *Statement to be relied upon must be got recorded:* If the Tribunal desires to rely upon a statement, it should formally call upon counsel for the assessee to record the statement in writing so as to enable the ITO to meet the case. *CIT v. Thayaballi Mulla Jeevaji Kapasi* 66 ITR 147.
2. *Fiscal matters must be disposed of expeditiously :* Law must move quickly not only in the Courts but also before the Tribunals and officers charged with the duty of expeditious administrative justice. Indeed administrative officers and Tribunals are taking much longer time than is necessary, thereby defeating the whole purpose of creating quasi-judicial Tribunals calculated to produce quick decisions especially in fiscal matters

ITO v. Ramnarayan Bhojnagarwala 103 ITR 797.

Statement of case to Supreme Court in certain cases [Sec. 257]

If, on an application made [against an order made under section 254 before the 1st day of October, 1998,] under section 256 the Appellate Tribunal is of the opinion that, on account of a conflict in the decisions of High Courts in respect of any particular question of law, it is expedient that a reference should be made direct to the Supreme Court, the Appellate Tribunal may draw up a statement of the case and refer it through its President direct to the Supreme Court.

Appeal to the High Court [Sec 260A & 260B]

An appeal shall lie to the High Court from every appellate order passed by the tribunal, if the High Court is satisfied that the case involves a substantial question of law. The appeal may be filed by the Commissioner or the assessee. The Memorandum of Appeal shall precisely state the substantial question of law involving the appeal. An appeal

along with a fee (as per Court Fees Act), shall be filed within 120 days of the date of receipt of the order appealed against. The question of law shall be formulated by the High Court, then the appeal shall be heard by a bench of at least two judges and decided by majority opinion. [Secs. 260A and 260B]

Case Laws :

1. Even if the High Courts have consistently taken an erroneous view, it would be worthwhile to let the matter rest, since large number of parties have modulated their legal relationship based on this settled position of law *Union of India v. Azadi Bachao Andolan* 132 Taxman 373/263 ITR 706.
2. *Revenue authorities to follow decision of jurisdictional High Court*: Revenue authorities within State cannot refuse to follow jurisdictional High Court's decision on ground that decision of some other High Court was pending disposal by Supreme Court *CIT v. G.M. Mittal Stainless Steel (P.) Ltd.* 130 Taxman 67/263 ITR 255.

Appeal to the Supreme Court [Sec. 261]

An appeal lies before the Supreme Court, against an order of the High Court in a reference, or in an appeal. Such appeal can be filed only if the High Court certifies it to be a fit case for appeal to the Supreme Court. If the High Court refuses to grant such a certificate, the assessee can file a Special Leave Petition before the Supreme Court. If the SLP is granted, the Supreme Court will hear and decide the appeal on merits. [Sec. 261]

Case Laws :

1. Certificate will not issue against judgment of single Judge: Under article 133(3) of the Constitution, no appeal shall lie to the Supreme Court from the judgment, decree or final order of one Judge of the High Court. Consequently, no certificate can be issued in respect of such a judgment, decree or order *State Bank of India v. State Bank of India Employees' Union* 169 ITR 675 .
2. Question must be of great public or private importance A certificate under section 261 which does not set out precisely the grounds or does not raise a question of great public or private importance does not comply with the requirements of the Act. The jurisdiction of the Supreme Court to entertain an appeal from the opinion recorded under the Act arises only when a certificate is properly issued by the High Court or when the Supreme Court grants special leave under article 136 of the Constitution. *India Machinery Stores (P.) Ltd. v. CIT* 78 ITR 50 ; *CIT v. Central India Industries Ltd.* 82 ITR 555 .

Hearing before Supreme Court. [Sec. 262]

- (1) The provisions of the Code of Civil Procedure, 1908 (5 of 1908), relating to appeals to the Supreme Court shall, so far as may be, apply in the case of appeals under section 261 as they apply in the case of appeals from decrees of a High Court :

Provided that nothing in this section shall be deemed to affect the provisions of sub-section (1) of section 260 or section 265.

- (2) The costs of the appeal shall be in the discretion of the Supreme Court.
- (3) Where the judgment of the High Court is varied or reversed in the appeal, effect shall be given to the order of the Supreme Court in the manner provided in section 260 in the case of a judgment of the High Court.

Case Law :

1. Question not raised earlier cannot be raised: An independent issue, not considered by Tribunal or High Court, could not be permitted to be raised for first time before Supreme Court *RM. Arunachalam v. CIT* 93 Taxman 423/227 ITR 222.



18.3 REVISION

Provisions relating to powers of revision of the Commissioner of Income Tax provides in sections 263 and 264 of the Income-tax Act which are analysed in a tabular form as under :

Section 263	Section 264
I. Scope:	
(a) Revision of order erroneous and prejudicial to the interest of revenue passed by the Assessing officer	Revision of other orders by any subordinate authority.
(b) Two circumstances must exist to enable the Commissioner to exercise the power of revision viz. (i) the order should be erroneous; and (ii) by virtue of the order being erroneous prejudice must have been caused to the interest and of the Revenue. CIT-vs.- Gabriel India Ltd., 203 ITR 108(Bom).	The Commissioner shall not revise any order where the appeal against the order is pending before the first or second appellate authorities (or) where the time for filing appeal has not lapsed the assessee has not waived his right of appeal.
II. Procedure :	
(a) Commissioner of Income Tax may call for and examine the records and revise the orders after hearing the assessee.	Commissioner of Income-tax either on his own motion or on an application by the assessee can call for the records and revise the order.
(b) Record shall include all records relating to any proceeding available at the time of examination of the file by the Commissioner of Income-tax.	Every application for revision should be accompanied by a fee ₹ 500.
III. Nature of order :	
(a) An order enhancing, modifying or cancelling the assessment can be passed by the Commissioner.	An order which is not prejudicial to the interest of the assessee can be passed.
(b) If the Income-tax Officer makes any mistake in carrying out the directions of the Appellate Assistant Commissioner or the Tribunal, his order can be revised by the Commissioner of Income Tax. Warner Lambert Co.-vs.- CIT, 205 ITR 395(Bom).	Commissioner declining to interfere will not amount to passing of an order prejudicial to the assessee.
(c) The Commissioner of Income Tax has jurisdiction and powers to initiate proceedings in respect of issues not touched by the CIT(Appeals) in his Appellate Order - CIT-vs.-Jayakumar B. Patil, 236 ITR 469(SC).	Where depreciation was not claimed before the Income-tax Officer or the Appellate Assistant Commissioner but was claimed or the first before the Commissioner of Income Tax in an application u/s. 264, the Commissioner must allow the claim on merits. Rashtriya Vikas Ltd. vs. CIT, 196 ITR 694(All.)
IV. Time limit :	
(a) No order can be passed after the expiry of 2 years from the end of the Financial Year in which the order to be revised was passed.	a) Commissioner cannot revise any order beyond 1 year period, b) Assessee cannot file an application after expiry of 1 year from the date of service of the order. Condonation of delay is possible if sufficient cause is shown.

(b) An order in revision may be passed at any time in the case of an order which has been passed in consequence of or to give effect to any finding or direction contained in an order of the Appellate Tribunal, the High Court or the supreme court.	Commissioner should pass an order disposing of the revision petition within one year from the end of the Financial Year n which the revision petition was filed by the assessee.
V. Remedy : Appeal can be filed to the Appellate Tribunal.	There is no right of appeal.

Tax to be paid notwithstanding reference, etc.[Sec. 265]

Notwithstanding that a reference has been made to the High Court or the Supreme Court or an appeal has been preferred to the Supreme Court, tax shall be payable in accordance with the assessment made in the case.

Execution for costs awarded by Supreme Court.[Sec. 266]

The High Court may, on petition made for the execution of the order of the Supreme Court in respect of any costs awarded thereby, transmit the order for execution to any court subordinate to the High Court.

[Amendment of assessment on appeal.[Sec . 267]

Where as a result of an appeal under section 246 [or section 246A] or section 253, any change is made in the assessment of a body of individuals or an association of persons or a new assessment of a body of individuals or an association of persons is ordered to be made, the Commissioner (Appeals) or the Appellate Tribunal, as the case may be, shall pass an order authorising the Assessing Officer either to amend the assessment made on any member of the body or association or make a fresh assessment on any member of the body or association.]

Exclusion of time taken for copy.[Sec. 268]

In computing the period of limitation prescribed for an appeal [or an application] under this Act, the day on which the order complained of was served and, if the assessee was not furnished with a copy of the order when the notice of the order was served upon him, the time requisite for obtaining a copy of such order, shall be excluded.

Definition of “High Court”.[Sec. 269]

In this Chapter,—

“High Court” means—

- (i) in relation to any State, the High Court for that State ;
- (ii) in relation to the Union territory of Delhi, the High Court of Delhi ;
- (iii) in relation to the Union territory of the Andaman and Nicobar Islands, the High Court at Calcutta ;
- (iv) in relation to the Union territory of [Lakshadweep], the High Court of Kerala;
- (v) in relation to the Union territory of Chandigarh, the High Court of Punjab and Haryana ;]
- (vi) in relation to the Union territories of Dadra and Nagar Haveli and Daman and Diu, the High Court at Bombay ; and
- (vii) in relation to the Union territory of Pondicherry, the High Court at Madras.]



STUDY NOTE - 19

INTEREST

This Study Note includes

- Provisions relating to Interest

19.1 INTEREST

Sections 234A, 234B and 234C provide for charging of mandatory interest since word 'shall' is used in the said sections. (CIT v. Anjum M.H. Ghaswala)

Interest For failure to deduct or pay any TDS [Sec. 201(A)]:

Where a person responsible for deducting tax at source does not deduct a source under Chapter XVII or after deducting tax fails to pay the same as required by Act, he is liable to pay interest @ 1% for every month or part of a month on the amount of such tax from the date on which tax deductible till the date it is actually paid.

Before furnishing the quarterly statement for each quarter in accordance with the provisions of sub-section (3) of section 200, such interest should be paid on self- assessment basis.

Interest for failure to collect any tax or pay TCS [Sec. 206C(7)] :

Where a person responsible for collecting tax at source under section 206C does not collect or after collecting tax fails to pay the same as required by Act, he is liable to pay interest @ 1% for every month or part of a month on the amount of such tax from the date on which tax should have been collected till the date it is actually paid.

Before furnishing the quarterly statement for each quarter in accordance with the provisions of sub-section (3) of section 200, such interest should be paid on self- assessment basis.

Interest on Delayed Payment of Tax other than Advance Tax [Sec. 220(2)]

Where an assessee fails to pay any tax, penalty, etc. within 30 days from the date of the Notice of Demand issued under Section.156, he shall be liable to pay interest on the outstanding demands @1% for every month or part of a month, for the period of default.

Where the Notice of Demand issued under section.156 is issued for payment of Advance Tax, interest is not chargeable on the outstanding demand, if any.

Penalty is prescribed under section 221 for any default in payment of advance tax, any other tax, penalty, etc. within 30 days from the date of the Notice of Demand issued under Section.156. Penalty can be to the extent of the amount of tax in arrears. However, where assessee has preferred, the AO can exercise his discretion so as to treat the assessee as not being in default in respect of nonpayment of tax on the amounts disputed in first appeal and then penalty under section 221 does not attract [Sec. 220(6)]

The following additional points should be considered :-

- Interest charged under Section.220 (2) is reduced in case of reduction of tax in appeal, rectification or revision.
- Interest under Section 220(2) is to be paid on delayed payments even if extension of time making payment has been granted.

Amount on which interest is payable:

- (i) Under Section 234A(1): Interest is payable on tax determined u/s 143(1) or on regular assessment u/s 143(3)/ 144/147/153A minus TDS/ Tax collected at source and advance tax paid by the assessee.
- (ii) Under Section 234A(3): Tax determined u/s 147 or 153A minus tax on total income determined u/s 143(1), 144 or 147 earlier.

No Interest if Taxes are paid :

Where the assessee had paid the taxes before the date of filling the return but could not file the return for reasons beyond his control but filled it belatedly, the charge of interest u/s 234A is not valid as in such cases there is no loss to the revenue. However interest would be payable where tax has not been deposited prior to the date of filling of the return. [Prannoy Roy (Dr.) v CIT 121 Taxman 314 (Del)]

For default in paying advance tax [Sec. 234B] :

Where an assessee who has failed to pay advance tax, interest @ 1% for every month or part of month is payable on assessed tax. Such interest is payable from April 1 of the assessment year to the date of determination of income under section 143(1) or on regular assessment.

Where an assessee who had paid advance tax but the amount of advance tax paid by him less than 90% of assessed tax, interest is payable @1% for every month or part of the month on the assessed tax minus advance tax is paid. Such interest is payable from April 1 of assessment year upto the date of determination of income u/s/ 143(1) or on regular assessment.

Any tax paid after 15th March but before 31st March is considered as advance tax paid.

Where, before the date of completion of regular assessment, tax is paid on the basis of self assessment under section 140 A or otherwise, the interest will be calculated as follows-

- (i) upto the date of payment of tax under section 140A or otherwise, interest will be calculated as mentioned earlier; and
- (ii) from the date of payment of tax under section 140A or otherwise, interest will be calculated on the amount by which advance tax and tax payment stated in (a) above falls short assessed tax.

The CBDT is empowered to relax the provisions of Sec. 234B in appropriate cases. [Sec. 119(2)(a)]

Interest for Deferment of Advance Tax [Sec. 234C]

An advance tax is said to have been deferred, if any one or more of the installments are not paid or tax paid is less than prescribed under the law. In case of such deferment of advance tax simple interest shall be payable as follows :

(i) For Assessee other than Companies :	
(a) If the tax paid upto 15th September is less than 30%	Simple interest on the amount of shortfall @1% p.m.for 3 months
(b) If the tax paid upto 15th December is less than 60%	– do –
(c) If the tax paid upto 15th March is less than 100% of the tax due	Simple interest on the amount of shortfall @ 1%.
(ii) For Company Assesseees :	
(a) If the tax paid upto 15th June is less than 15%	Simple interest on the amount of shortfall @1% p.m. for 3 months
(b) If the tax paid upto 15th September is less than 45%	– do –
(c) If the tax paid upto 15th December is less than 75%	– do –
(d) If the tax paid upto 15th March is less than 100%	Simple interest on the amount of shortfall @ 1% for 1 month



No interest under section 234C is leviable where the shortfall in payment of advance tax installments is on account of under-estimate/non-estimate of any capital gains or winning from lotteries, crossword puzzles, races, etc. This concession of not charging of interest is applicable where such incomes arise after payment of any of the installments and the whole tax on the items of income stated herein before is deposited along with the next succeeding installment falling due after the income arose.

Interest for Failure to pay Advance Tax [Sec. 234B and 234C]

Interest under sections 234B and 234C is payable even in cases where the assessee fails to pay advance tax at all. Any tax paid after 15th March but before 31st March is considered as advance tax paid.

INTEREST IS PAYABLE TO ASSESSEE ON REFUND [Sec. 244A]

Interest on excess payment of advance tax, tax deducted or collected at source and any other tax or penalty becoming refundable shall be paid @ 1/2% for every month or part of a month. The period for which the interest is payable will be:

- (i) For refund out of advance and tax deducted at source, from 1st April of relevant assessment year to the date on which the refund is granted. However, no interest is payable, if the amount of refund is less than 10% of the tax determined under section 143(1) or on regular assessment or assessment of FBT under section 115WE, and
- (ii) For all other tax or penalties, from the date of payment of tax or penalty to the date on which the refund is granted.

Delay in granting refund attributable to the assessee is excluded from the period for which interest is payable. Where the amount on which interest was payable is increased or decreased due to regular assessment orders, reassessment, rectification, appeals, revision or Settlement Commission's order, interest is also will be increased or decreased.

Interest earned by assessee under section 244A is treated as taxable income of the previous year in which it is allowed.

ROUNDING OFF OF MONTH [Rule 119A]

The interest is to be calculated, any fraction of a month deemed to be full month and the interest shall be so calculated.

ROUNDING OFF OF AMOUNT [Rule 119A]

The amount of tax, penalty or other sum in respect of which interest is to be calculated is to be rounded off to the nearest multiple of ₹ 100 and for this purpose any fraction of ₹ 100 is to be ignored.

ILLUSTRATIONS ON INTEREST u/s 234A, 234B & 234C

Illustration 1. A firm made the following payments of advance tax during the Financial Year 2011-12 :

	Figures in ₹ Lakhs
15.09.2011	9.30
15.12.2011	9.0
15.03.2012	<u>13.9</u>
	<u>32.20</u>

The income returned by the firm is ₹ 100 Lakhs under the head “Business” and ₹ 10 Lakhs by way of Long-term Capital Gains on sale of a property effected on 1.3.2012. What is the interest payable by the assessee u/s 234B and 234C of the Income Tax Act for Assessment Year 2012-2013? Assume that the return of income was filed on 31.07.2012 and tax was fully made upon self-assessment.

Solution :

Assessee : Firm

Previous Year : 2011-2012

Assessment Year : 2012-2013

(a) **Interest u/s 234B = Nil** [since more than 90% of Tax Payable has been paid before the end of the previous year]

(b) **Interest u/s 234C**

Due date	Advance Tax Payable ₹	Advance Tax paid ₹	Cumulative Advance Tax paid before due date ₹	Shortfall in Payment ₹	Surplus ₹	Months	Interest @ 1% p.m. ₹
15.9.2011	30% of ₹ 30,90,000 = 9,27,000	9,00,000	9,30,000	—	3,000	—	—
15.12.2011	60% of ₹ 30,90,000 = 18,54,000	9,00,000	18,30,000	24,000	—	3	720
15.3.2012	100% of ₹ 32,96,000 = 32,96,000	13,90,000	32,20,000	76,000	—	1	760
							1,480

Note : Tax on LTCG has been considered only for the 3rd instalment as such gain had arisen only on 1.3.2011.

Computation of Actual Tax Payable by the Firm :

Particulars	₹	₹
Profits and Gains of Business or Profession		1,00,00,000
Capital Gains — Long Term Capital Gain		10,00,000
Total Income		1,10,00,000
Tax on Total Income including Surcharge and Cess		
On Long Term Gain of ₹ 10 lakhs @ 20%+ EC @ 2%+ SHEC @ 1%	2,06,000	
On Business Income @ of ₹ 100 lakhs @ 30%+ EC @ 2%+ SHEC @ 1%	30,90,000	
Net Tax Payable		32,96,000

Note : Tax on Business income alone considered for computation of 1st and 2nd instalment.

Illustration 2. A firm made the following payments of advance tax during the previous year 2011-12 :

	₹ in lakh
September 15, 2011	7.00
December 15, 2011	7.75
March 15, 2012	13.00
	<u>27.75</u>

The return of income is filed on 31.7.2012 showing —

Bonus income ₹ 80 lakh

Long term capital gain taxable @ 20% (as on 1.12.2011) ₹ 20 lakh

Compute interest payable u/s 234C.

Solution :

Computation of tax liability for the A.Y. 2012-13.

	₹ in lakh	
Particulars	Business Income	Long term capital gain
Income	80.00	20.00
Tax rate	30%	20%
Tax liability before surcharge	24.00	4.00
Add : Education Cess & SHEC	0.72	0.12
Tax liability including cess	24.72	4.12

∴ Total Tax Liability = (24.72 + 4.12) lakhs = ₹ 28.94 lakhs.

Computation of interest payable u/s 234

Due date	Advance Tax Payment ₹	Advance Tax paid ₹	Cumulative Advance Tax paid before due date ₹	Shortfall in Payment ₹	Surplus ₹	Months	Interest @ 1% p.m. ₹
15.9.2011	30% of ₹ 24,72,000 = 7,41,600	7,00,000	7,00,000	41,600	—	3	1,248
15.12.2011	60% of ₹ 24,72,000 = 14,83,200 (+) 60% of 4,12,000 = 2,47,200	7,75,000	14,75,000	2,55,400	—	3	7,662
15.3.2012	100% of ₹ 28,94,000 = 28,94,000	13,00,000	27,75,000	1,19,000	—	1	1,190
							10,100

Illustration 3. In the case of Ms Laxmi, you are required to compute the interest u/s 234A, 234B & 234C from the following details—

Tax on total income ₹ 2,00,000; Due date for filing the return 30.09.2012; Actual date of filing the return 1.10.2013 and tax paid on 30.09.2012 ₹ 2,00,000.

Solution :

Computation of interest u/s 234A

Particulars	As per assessed income	
Tax		₹ 2,00,000
Less : Advance tax paid	Nil	
TDS	Nil	Nil
Amount on which interest is payable		₹ 2,00,000
Period of default (October being part of a month shall be considered)		1 month
Interest u/s 234A (1% × ₹ 2,00,000 × 1 month)		₹ 2,000

Computation of interest u/s 234B

Since assessee did not pay any amount by way of advance tax, hence she is liable to pay interest u/s 234B.

Particulars	Assessed income
Shortfall	₹ 2,00,000
Period of default (From April to September)	6 months
Interest (1% × 2,00,000 × 6 months)	₹ 2,000

Computation of interest u/s 234A

Due date	Advance Tax Payment	Advance Tax paid	Cumulative Advance Tax paid before due date	Shortfall in Payment	Surplus	Months	Interest @ 1% p.m.
	₹	₹	₹	₹	₹		₹
15.9.2011	30% of ₹ 2,00,000 = 60,000	Nil	Nil	60,000	—	3	1,800
15.12.2011	60% of ₹ 2,00,000 = 1,20,000	Nil	Nil	1,20,000	—	3	3,600
15.3.2012	100% of ₹ 2,00,000 = 2,00,000	Nil	Nil	2,00,000	—	1	2,000
							7,400

Total interest payable

Particulars	Amount
U/s 234A	2,000
U/s 234B	12,000
U/s 234C	7,400
Total	21,400

Illustration 5. During the previous year 2011-12, Mrs. X (aged 46 years) pays the following instalments of advance tax :

	₹
On September 15, 2011	6,000
On December 15, 2011	14,000
On March 15, 2012	16,000
On March 16, 2012	18,000

Mrs. X files return of ₹ 7,01,000. Assessment is also completed on the basis of income returned by Mrs. X after making addition of ₹ 25,000 (date of assessment order : January 20, 2013). Mrs. X is entitled to tax credit of ₹ 12,510 on account of tax deducted at source. Compute interest under sections 234B and 234C.

Solution :

Interest liability under section 234B

	₹
Income (7,01,000 + 25,000) =	7,26,000
Tax on ₹ 7,26,000	76,200
Less : Tax deducted at source	12,510
Assessed tax	63,690
90% of assessed tax	57,321

Advance tax paid during 2011-12 (i.e., ₹ 6,000 + 14,000 + 16,000 + 18,000) = ₹ 54,000.

Since advance tax during the previous year 2011-12 is less than 90% of assessed tax, Mrs. X is liable to pay interest under section 234B, i.e., on the shortfall of ₹ 9,690 (being ₹ 63,690 – 54,000) for 10 months (₹ 9,690 × 1/100 × 10) which comes to ₹ 969.

Interest liability under section 234C :

Tax on ₹ 7,01,000 =

Due date	Advance Tax Payment	Advance Tax paid	Cumulative Advance Tax paid before due date	Shortfall in Payment	Surplus	Months	Interest @ 1% p.m.
	₹	₹	₹	₹	₹		₹
15.9.2011	30% of ₹ 71,200 = 21,360	6,000	6,000	15,360	—	3	461
15.12.2011	60% of ₹ 71,200 = 42,720	14,000	20,000	22,720	—	3	682
15.3.2012	100% of ₹ 71,200 = 71,200	34,000	54,000	17,000	—	1	172
							1,315

STUDY NOTE - 20

ADVANCE PAYMENT OF TAX

This Study Note includes

- Provisions relating to Advance Payment of Tax

SECTION 4: TAX PAYABLE BY AN ASSESSES SHALL BE PAID IN ADVANCE

Who is liable to pay advance tax (Section 208)	When the advance tax-payable by any person for the assessment year immediately following the financial year is ₹ 10,000 or more.	
Amount of Advance Tax payable	Tax on Total Income Less: Rebate and relief Add: Surcharge Less: Tax deducted at source and Tax collected at source.	
Due Date of Installment in a relevant previous year	Amount payable by Corporate Assesses	Amount payable by Non-Corporate Assesses
On or before June 15	15% of Advance tax payable	Not Applicable
On or before September 15	45% of Advance tax payable	30% of Advance tax payable
On or before December 15	75% of Advance tax payable	60% of Advance tax payable
On or before March 15	100% of Advance tax payable	100% of Advance tax payable

Note :

- Any amount paid by way of advance tax on or before 31st March of the relevant previous year shall also be treated as advance tax paid during the financial year ending on that day.
- If the due date of payment of advance tax is a banking holiday, the Assessee can make the payment on the next immediately following working day. In such cases, no interest shall be leviable u/s 234B or 234C.

COLLECTION OF TAX

PROCEDURE FOR PAYMENT OF TAX UNDER A DEMAND NOTICE ISSUED u/s 156

- Due date for payment of tax [Section 220(1)]:** Any amount of tax other than advance tax specified as payable in a notice of demand u/s 156 shall be paid within 30 days.
- Reduction of time limit:** If the Assessing Officer has any reason to believe that it would be detrimental to revenue if the full period of 30 days as aforesaid is allowed, he may, with the previous approval of the Joint Commissioner, direct that the sum is to be paid within any period less than 30 days.
- Extension of time limit:** The Assessing Officer may extend the time on the basis of an application made by the Assessee to pay the tax demanded u/s 156(1) or allow payments by installments subject to conditions as he may think fit to impose.

CIRCUMSTANCES OF ASSESSEE BE TREATED AS DEEMED TO BE IN DEFAULT

- Assessee deemed to be in default [Section 220 (4)]:** The Assessee shall be deemed to be in default if the amount specified in the notice u/s 156 is not paid within the time allowed or within such extended time u/s 220(3).



2. **Amount of default [Section 220(5)]** Where the payment is allowed by instalments, the amount of default shall be the amount outstanding. All the other instalments shall be deemed to be in default on the same date as the instalment actually in default.
3. **Circumstances under which the Assessee is not deemed to be in default:**
 - (a) If the Assessee presents an appeal to the CIT (Appeals), the Assessing Officer may, in his discretion and subject to such conditions as he may think fit to impose, treat the Assessee as not being in default as long as the appeal is not disposed of. **[Section 220(6)]**
 - (b) Where the income of an Assessee arising in India is assessed in a Country where the laws prohibit or restrict the remittance of money to India, such an Assessee shall not be treated as Assessee in default in respect of tax due on the income which cannot be brought into India. **[Section 220(7)]**
 - (c) Where the demand in dispute has arisen because the Assessing Officer has adopted an interpretation of law in respect of which there are conflicting High Court decisions and the Department has not accepted the interpretation of the Court, the Assessee shall not be deemed in default. **[Circular No.530/6-3-1989]**
 - (d) Where the demand in dispute relates to issues which are decided earlier in the Assessee's favour by an appellate authority / Court in his own case (say, for preceding assessment years), the Assessee shall not be deemed to be in default to the extent of tax liability relating to such disputed points. **[Circular No.530/6-3-1989]**

CONSEQUENCES OF NON-PAYMENT OR DELAY IN PAYMENT AT TAX AS DEMANDED BY NOTICE u/s 156

Interest for belated payment of tax: **[Section 220(2)]**

1. **Interest** : If the amount demanded as per notice u/s 156 is not paid within the period specified in that notice, the Assessee shall be liable to pay a simple interest @ 1 % per month or part of a month.
2. **Period of Interest** : The period of interest shall be from the day immediately following the end of the period mentioned in the notice ending with the day on which the amount is paid,
3. **Penalty** : **[Section 221]**
 - (a) Where the Assessee is in default or deemed to be in default in making payment of tax, the Assessing Officer may direct the Assessee to pay a penalty not exceeding the amount of tax in arrears,
 - (b) Penalty may be levied even if the tax is paid belatedly but before the levy of such penalty.
4. **Opportunity to Assessee** : The Assessee shall be given a reasonable opportunity of being heard.
5. **No penalty** : In case the Assessee proves to the satisfaction of the Assessing Officer that the default was for good and sufficient reasons, no penalty shall be levied.
6. **Refund of penalty** : In case the amount of tax was wholly reduced in any final order, then the penalty levied shall be cancelled and amount of penalty paid shall be refunded.

RECOVERY OF TAX

CERTIFICATE OF RECOVERY u/s 222(1)

1. **Certificate of Recovery [Section 222(1)]** : When an Assessee is in default or deemed to be in default in payment of tax, the Tax Recovery Officer may draw up a statement under his signature in Form No.57 specifying the amount of arrears due from the Assessee. Such a statement is called Certificate.
2. The Assessee cannot dispute the correctness of any certificate drawn up by the TRO on any ground. **[Section 224]**
3. It is lawful on the part of the TRO to cancel the certificate for any reason he thinks necessary so to do or to correct any clerical or arithmetical mistake therein. **[Section 224]**

MODES OF RECOVERY OF TAX UNDER THE PROVISIONS OF THE ACT, BY THE TAX RECOVERY OFFICER

1. **Modes of Recovery of tax [Section 222]**: In accordance with the rules laid down in the Second Schedule, the amount specified in the certificate may be recovered by any one or more of the following modes -
 - (a) Attachment and sale of the Assessee's movable property,

- (b) Attachment and sale of the Assessee's immovable property,
 - (c) Arrest of the Assessee and his detention in prison,
 - (d) Appointing a receiver for the management of the Assessee's movable and immovable properties.
2. **Movable and immovable property includes** any property which has been transferred directly or indirectly by the Assessee to his spouse or minor child or son's wife or son's minor child for inadequate consideration and the same is held by such persons.
 3. **Property held by major:** Any movable property or immovable property transferred to the minor child or son's minor child shall be treated as the Assessee's property even after the minor attains majority.
 4. The Tax Recovery Officer may take action u/s 222(1) for recovery of tax arrears even though any other proceedings for recovery of arrears have been taken,

OTHER MODES OF RECOVERY [Section 226]:

1. **Applicability:** Section 226 is applicable in the following situations:
 - (a) No certificate u/s 222 has been drawn by the Assessing Officer
 - (b) Where a certificate has been drawn u/s 226, the Tax Recovery Officer, without any Prejudice to the modes of recovery specified in Section 222, can recover by any one or more of the other modes u/s 226.
2. **Modes of Recovery:**

Mode	Tax arrears due from	Arrears of tax to be deducted by	payment Of sum deducted	Other Provisions
Attachment Of Salary [Section 226(2)]	Salaried Employee	Person paying salary to such person	To the credit of Central Government	Not applicable where the salary is exempt from attachment under the Code of Civil Procedure
Garnishee Order (Section 226(3))	Any Assessee	Any Person from whom money is due or may become due to the Assessee or any person who holds any money for the Assessee jointly with any other person	To the credit of Central Government	Refer Pt.3 Below
Recovery from money belonging to Assessee lying in Courts custody [Section 226(4)]	Assessee whose money is in Courts custody	Court	To the AO or TRO to the extent of liability	—
Recovery of arrears of tax of tax by distraint and sale [Section 226(5)]	Any Assessee	Not Applicable	Not Applicable	It should be authorized by the CIT/CCIT by general or special order. The distraint or sale shall be made in the manner as that for an attachment and sale of movable Property attachable by actual seizure

ILLUSTRATIONS ON ADVANCE TAX

Illustration 1. Compute the Advance Tax payable by R from the following estimated income submitted for the previous year 2011-12.

	₹
(1) Income from Salary	3,64,000
(2) Rent from house property (per annum)	1,80,000
(3) Interest on Government securities	5,000
(4) Interest on bank deposits	3,000
(5) Receipt from horse race (net)	14,000
(6) Agricultural Income	90,000
(7) Contribution towards PPF	10,000

Tax deducted at source by the employer on salary is ₹ 9,680.

Solution :

Computation of Estimated Total Income for the Previous Year 2011-12

	₹	₹
Income from Salary :		
Gross salary	3,64,000	
Less : Deduction	Nil	3,64,000
Income from House Property :		
Rent received	1,80,000	
Less : (Statutory deduction u/s 24(a) @ 30%)	54,000	1,26,000
Income from Other Sources :		
Interest on Government securities	5,000	
Interest on Bank Deposit	3,000	
Horse Races (Gross)	20,000	28,000
Estimated Gross Total Income		5,18,000
Less : Deduction under section 80C		10,000
		5,08,000
Estimated Tax :		
Step-1 : Aggregate of Agricultural income + Non-Agricultural income (90,000 + 5,08,000) = 5,98,000		
Tax on : Income from Horse Race of ₹ 20,000 @ 30%	6,000	
Balance income of ₹ 5,78,000	47,600	53,600
Step-2 : Aggregate of Basic exemption limit of agricultural income (1,80,000 + 90,000) = 2,70,000		
Tax on ₹ 2,70,000		9,000

Step-3 : Tax on non-agricultural income		
Tax under step-1 - Tax under step-2 (53,600 – 9,000) = 44,900		
Estimated tax payable		44,900
Add : Education cess @ 2%		898
Add : SHEC @ 1%		449
		<u>46,247</u>
Less : Estimated TDS		
on salary	9,680	
on horse races	6,000	15,680
	<u></u>	<u>30,567</u>
Advance tax payable (rounded off)		9,170
First installment payable by 15.9.2011 (30%)		9,170
Second installment payable by 15.12.2011 (30%)		12,227
Third installment payable by 15.3.2012 (balance 40%)		

Working notes :

Computation of gross winnings from horse races :	₹
Net Amount	14,000
Grossing up $14,000 \times \frac{100}{70}$	<u>20,000</u>
Tax deducted at source (Gross amount ₹ 20,000 – Amount received ₹ 14,000)	<u>6,000</u>

Illustration 2. X Ltd. estimates its income for the previous year 2010-11 at ₹ 1,20,000. Besides this income, it has also earned long-term capital gain of ₹ 80,000 on transfer of gold on 1.12.2011. Compute the advance tax payable by the company in various instalments.

Solution :

	₹
Tax on ₹ 1,20,000 @ 30%	36,000
LTCG of ₹ 80,000 @ 20%	<u>16,000</u>
	52,000
Add : Education cess @ 2%	1,040
SHEC @ 1%	<u>520</u>
	<u>53,560</u>

Amount payable on 1st and 2nd instalment

For the first two instalments tax on LTCG will not be taken into account as this accrued on 1.12.2011 i.e. after the due date of the first 2 instalments.

	₹
Tax including Education Cess and SHEC payable	
without Long-term Capital Gain (₹ 36,000 + 720 + 360)	<u>37,080</u>

Advance Tax Payable

Due Date	Tax Liability as on due date	Amount of Instalment Payable (₹)
15.6.2011	15% of 37,080 = 5,562	₹ 5,562
15.9.2011	45% of 37,080 = 16,680	= 16,680 – 5,560 = 11,118
15.12.2011	75% of 53,560 = 40,170	= 40,170 – 5,562 – 11,118 = 23,490
15.3.2012	100% of 53,560 = 53,560	= 53,560 – 5,562 – 11,118 – 23,490 = 13,390

Illustration 3. Find out the amount of advance tax payable by ABC Ltd. on specified dates for the previous year 2011-12 :

Business income	₹ 1,75,000
Long term capital gain on 31-7-2011	₹ 3,50,000
Bank interest	₹ 10,000
TDS on business income	₹ 19,995

Solution :

Computation of Total Income of ABC Ltd. for the previous Year 2010-11

Particulars	Amount ₹
Profits and gains of business or profession	1,75,000
Capital gains: Long term capital gains	3,50,000
Income from other sources: Bank Interest	10,000
Total Income	5,35,000

Computation of tax liability of ABC Ltd. for the previous year 2011-12

Particulars	Long term capital gain ₹	Other income ₹
Income	3,50,000	1,85,000
Tax rate	20%	30%
Tax on above	70,000	55,500
Add : Education cess & SHEC	2,100	1,665
Tax and cess payable	72,100	57,165
Less : TDS	—	19,995
Advance tax payable	72,100	37,170

Advance tax to be paid on specified dates

Date	Advance tax on LTCG		Advance tax on income other than LTCG		Total (a+b) ₹
	Workings	Amount (a) ₹	Workings	Amount (b) ₹	
15.06.2011	As LTCG occurred on 31.7.11	Nil	15% of ₹ 37,170	5,576	5,576
15.09.2011	45% of ₹ 72,100	32,445	30% of ₹ 37,170	11,151	43,596
15.12.2011	30% of ₹ 72,100	21,630	30% of ₹ 37,170	11,151	32,781
15.03.2012	25% of ₹ 72,100	18,025	25% of ₹ 37,170	9,292	27,317
Total		72,100		37,170	1,09,270

Illustration 4. Find out the amount of advance tax payable by Mr. A on specified dates under the Income tax Act, 1961 for the Previous Year 2011-12 :

	₹
Business income	2,75,000
Long term capital gain on 31-7-2011	60,000
Winning from lotteries on 12-9-2011	50,000
Bank interest	10,000
Other income	5,000
Investment in PPF	40,000
Tax deducted at source :	
Case I	48,000
Case II	25,000

Solution :

Computation of Total Income of Mr. A for the previous year 2011-12 :

Particulars	Details	Amount
Profits and gains of business or profession		2,75,000
Capital gains : Long term capital gains		1,60,000
Income from other sources		
Winning from lotteries	50,000	
Bank interest	10,000	
Other income	5,000	65,000
Gross Total Income		5,00,000
Less : Deduction u/s 80C — Deposits in PPF		40,000
Total Income		4,60,000

Computation of Tax liability of Mr. A for the previous year 2011-12 :

Income	Case 1	Case 2
Long term capital gain (₹ 1,60,000 @ 20%)	32,000	32,000
Winning from lotteries (₹ 50,000 @ 30%)	15,000	15,000
Balance income (₹ 2,50,000)	9,000	9,000
Tax	56,000	56,000
Add : Education cess & SHEC	1,680	1,680
	57,680	57,680
Less : Tax Deducted at Source	48,000	25,000
Total Tax Payable	9,680	32,680

Advance tax to be paid on specified dates —

Case I : Since amount of tax payable is less than ₹10000, assessee is not liable to pay advance tax.		
Case II : Advance Tax Payable		
Due Date	Tax Liability (₹)	Amount of Instalment (₹)
15.6.2011	30% of 32,680 = 9,804	9,804
15.9.2011	60% of 32,680 = 19,608	= 19,608 – 9,804 = 9,804
15.12.2011	100% of 32,680 = 32,680	= 32,680 – 9,804 – 9,804 = 13,072



STUDY NOTE - 21

COLLECTION AND RECOVERY OF TAX

This Study Note includes

- Provisions relating to Collection and Recovery of Tax

COLLECTION AND RECOVERY OF TAX

21.1 WHEN TAX PAYABLE AND WHEN DEMAND IN DEFAULT [Sec. 220]

Any amount specified as payable in a notice of demand u/s. 156 shall be paid within 30 days of the service of the notice at the place and to the person mentioned in the notice. Where the A.O. has any reason to believe that it will be detrimental to revenue if full period of 30 days is allowed, he may, with the previous approval of the Deputy Commissioner, direct the sum specified in the notice of demand to be paid within such period being a period less than 30 days.

Where the amount specified in any notice of demand u/s. 156 is not paid within the period of 30 days, the assessee shall be liable to simple interest @1.5% for every month or part of a month comprised in the period commencing from the immediately following the end of the period and ending with the day on which the amount is paid.

However, the Chief Commissioner or Commissioner may reduce or waive the amount of interest if he is satisfied that the payment of such amount would cause genuine hardship to the assessee, the default in the payment of the amount on which interest was payable was due to circumstances beyond the control of the assessee and the assessee cooperated in any enquiry relating to the assessment or any proceeding for the recovery of amount due from him.

However, the Assessing Officer may, on an application made by the assessee before the due date of payment of tax, extend the time for payment or allow payment by installments, subject to such conditions as he may think fit. If the amount is not paid within the time limit of 30 days or within the extended time limit, the assessee shall be deemed to be in default.

Case Law:

(i) If tax is refunded pursuant to first appeal, but later restored and paid in second appeal, interest cannot be levied on refund made. *Vikrant Tyres Ltd. v. First ITO* 247 ITR 821.

21.2 PENALTY PAYABLE WHEN TAX IS IN DEFAULT [Sec. 221]

When an assessee is in default, he shall, in addition to the amount of the arrears and the amount of interest payable u/s. 220(2), be liable to pay penalty such amount as the A.O. may direct and in case of continuing default, such further amount as the A.O. may direct, so, however, that the total amount of penalty does not exceed the amount of in arrears.

21.3 CERTIFICATE TO TAX RECOVERY OFFICER [Sec. 222]

In the case of default of an assessee, the Tax Recovery Officer may draw up a statement (called certificate) in the prescribed form specifying the amount of arrears due from the assessee and proceed to recover by one or more of the following modes-

- attachment and sale of assessee's movable property;
- attachment and sale of assessee's immovable property;
- arrest of the assessee and his detention in prison
- appointing a receiver for the management of the assessee's movable and imovable properties.

Case Law:

(i) Recovery proceedings can be taken against the legal representatives - *First Addl. ITO v. T.M.K. Abdul Kassim* 46 ITR 149 .

[Tax Recovery Officer by whom recovery is to be effected. [Sec. 223]

- (1) The Tax Recovery Officer competent to take action under section 222 shall be—
 - (a) the Tax Recovery Officer within whose jurisdiction the assessee carries on his business or profession or within whose jurisdiction the principal place of his business or profession is situate, or
 - (b) the Tax Recovery Officer within whose jurisdiction the assessee resides or any movable or immovable property of the assessee is situate, the jurisdiction for this purpose being the jurisdiction assigned to the Tax Recovery Officer under the orders or directions issued by the Board, or by the Chief Commissioner or Commissioner who is authorised in this behalf by the Board in pursuance of section 120.
- (2) Where an assessee has property within the jurisdiction of more than one Tax Recovery Officer and the Tax Recovery Officer by whom the certificate is drawn up—
 - (a) is not able to recover the entire amount by sale of the property, movable or immovable, within his jurisdiction, or
 - (b) is of the opinion that, for the purpose of expediting or securing the recovery of the whole or any part of the amount under this Chapter, it is necessary so to do, he may send the certificate or, where only a part of the amount is to be recovered, a copy of the certificate certified in the prescribed manner and specifying the amount to be recovered to a Tax Recovery Officer within whose jurisdiction the assessee resides or has property and, thereupon, that Tax Recovery Officer shall also proceed to recover the amount under this Chapter as if the certificate or copy thereof had been drawn up by him.]

Validity of certificate and cancellation or amendment thereof [Sec. 224]

It shall not be open to the assessee to dispute the correctness of any certificate drawn up by the Tax Recovery Officer on any ground whatsoever, but it shall be lawful for the Tax Recovery Officer to cancel the certificate if, for any reason, he thinks it necessary so to do, or to correct any clerical or arithmetical mistake therein.]

Stay of proceedings in pursuance of certificate and amendment or cancellation thereof [Sec. 225]

- (1) It shall be lawful for the Tax Recovery Officer to grant time for the payment of any tax and when he does so, he shall stay the proceedings for the recovery of such tax until the expiry of the time so granted.
- (2) Where the order giving rise to a demand of tax for which a certificate has been drawn up is modified in appeal or other proceeding under this Act, and, as a consequence thereof, the demand is reduced but the order is the subject-matter of further proceeding under this Act, the Tax Recovery Officer shall stay the recovery of such part of the amount specified in the certificate as pertains to the said reduction for the period for which the appeal or other proceeding remains pending.
- (3) Where a certificate has been drawn up and subsequently the amount of the outstanding demand is reduced as a result of an appeal or other proceeding under this Act, the Tax Recovery Officer shall, when the order which was the subject-matter of such appeal or other proceeding has become final and conclusive, amend the certificate, or cancel it, as the case may be.]

21.4 OTHER MODES OF RECOVERY [Sec. 226]

If any assessee is in receipt of any income chargeable under the head “salaries”, the Assessing Officer, Tax Recovery Officer may require any person paying the same to deduct from any payment subsequent to the date of such requisition any arrears of tax due from such assessee, and such person shall comply with any such requisition and shall pay the sum so deducted to the credit of the Central Government or as the Board directs.



The Assessing Officer or Tax Recovery Officer may, if authorised by the Chief Commissioner or Commissioner by general or special order, recover any arrears of tax due from an assessee by distraint and sale of his movable property in the manner laid down in the Third Schedule.

Case Laws:

- (i) ITO can simultaneously take action under section 156 and section 226. *Third ITO v. M. Damodar Bhat* 71 ITR 806.
- (ii) A garnishee order could be passed only if income-tax had been assessed and had remained unpaid - *All India Reporter Ltd. v. Ramchandra D. Datar* 41 ITR 446.

21.5 RECOVERY THROUGH STATE GOVERNMENT [Sec. 227]

If the recovery of tax in any area is entrusted to a State Government under Act. 258(1) of the Constitution of India, then State Government may direct, with respect to that area or any part thereof, that tax shall be recovered therein with, and as an addition to, any municipal tax or local rate is recovered.

Recovery of tax in pursuance of agreements with foreign countries [Sec. 228A]

(1) Where an agreement is entered into by the Central Government with the Government of any country outside India for recovery of income-tax under this Act and the corresponding law in force in that country and the Government of that country or any authority under that Government which is specified in this behalf in such agreement sends to the Board a certificate for the recovery of any tax due under such corresponding law from a person having any property in India, the Board may forward such certificate to any Tax Recovery Officer within whose jurisdiction such property is situated and thereupon such Tax Recovery Officer shall—

- (a) proceed to recover the amount specified in the certificate in the manner in which he would proceed to recover the amount [specified in a certificate drawn up by him under [section 222](#)]; and
- (b) remit any sum so recovered by him to the Board after deducting his expenses in connection with the recovery proceedings.

(2) Where an assessee is in default or is deemed to be in default in making a payment of tax, the Tax Recovery Officer may, if the assessee has property in a country outside India (being a country with which the Central Government has entered into an agreement for the recovery of income-tax under this Act and the corresponding law in force in that country), forward to the Board a certificate drawn up by him under [section 222](#) and the Board may take such action thereon as it may deem appropriate having regard to the terms of the agreement with such country.

21.6 RECOVERY OF PENALTIES, FINE, INTEREST AND OTHER SUMS [Sec. 229]

Any sum imposed by way of interest, fine, penalty or any other sum payable under the provisions of this Act, shall be recoverable in the manner provided in this Chapter for the recovery of arrears of tax as stated earlier.

Tax clearance certificate [Sec. 230]

(1) Subject to such exceptions as the Central Government may, by notification in the Official Gazette, specify in this behalf, no person,—

- (a) who is not domiciled in India;
- (b) who has come to India in connection with business, profession or employment; and
- (c) who has income derived from any source in India, shall leave the territory of India by land, sea or air unless he furnishes to such authority as may be prescribed—
 - (i) an undertaking in the prescribed form from his employer; or
 - (ii) through whom such person is in receipt of the income,

to the effect that tax payable by such person who is not domiciled in India shall be paid by the employer referred to in clause (i) or the person referred to in clause (ii), and the prescribed authority shall, on receipt of the undertaking, immediately give to such person a no objection certificate, for leaving India:

Provided that nothing contained in sub-section (1) shall apply to a person who is not domiciled in India but visits India as a foreign tourist or for any other purpose not connected with business, profession or employment.

(1A) Subject to such exceptions as the Central Government may, by notification in the Official Gazette, specify in this behalf, every person, who is domiciled in India at the time of his departure from India, shall furnish, in the prescribed form to the income-tax authority or such other authority as may be prescribed—

- (a) the permanent account number allotted to him under section 139A:

Provided that in case no such permanent account number has been allotted to him, or his total income is not chargeable to income-tax or he is not required to obtain a permanent account number under this Act, such person shall furnish a certificate in the prescribed form;

- (b) the purpose of his visit outside India;
(c) the estimated period of his stay outside India:

Provided that no person—

- (i) who is domiciled in India at the time of his departure; and
(ii) in respect of whom circumstances exist which, in the opinion of an income-tax authority render it necessary for such person to obtain a certificate under this section,

shall leave the territory of India by land, sea or air unless he obtains a certificate from the income-tax authority stating that he has no liabilities under this Act, or the Wealth-tax Act, 1957 (27 of 1957), or the Gift-tax Act, 1958 (18 of 1958), or the Expenditure-tax Act, 1987 (35 of 1987), or that satisfactory arrangements have been made for the payment of all or any of such taxes which are or may become payable by that person :

Provided that no income-tax authority shall make it necessary for any person who is domiciled in India to obtain a certificate under this section unless he records the reasons therefor and obtains the prior approval of the Chief Commissioner of Income-tax.]

- (2) If the owner or charterer of any ship or aircraft carrying persons from any place in the territory of India to any place outside India allows any person to whom sub-section (1) [or the first proviso to sub-section (1A)] applies to travel by such ship or aircraft without first satisfying himself that such person is in possession of a certificate as required by that sub-section, he shall be personally liable to pay the whole or any part of the amount of tax, if any, payable by such person as the [Assessing] Officer may, having regard to the circumstances of the case, determine.
- (3) In respect of any sum payable by the owner or charterer of any ship or aircraft under sub-section (2), the owner or charterer, as the case may be, shall be deemed to be an assessee in default for such sum, and such sum shall be recoverable from him in the manner provided in this Chapter as if it were an arrear of tax.
- (4) The Board may make rules for regulating any matter necessary for, or incidental to, the purpose of carrying out the provisions of this section.

Explanation.—For the purposes of this section, the expressions “owner” and “charterer” include any representative, agent or employee empowered by the owner or charterer to allow persons to travel by the ship or aircraft.

21.7 RECOVERY BY SUIT OR UNDER ANY LAW NOT AFFECTED [SEC. 232]

The different modes of recovery specified earlier shall not affect in any way —

- (a) any other law for the time being in force relating to the recovery of due to the Government; or
(b) the right of the Government to institute a suit for the recovery of the arrears due from the assessee; and it shall be lawful for the A.O. or the Government, as the case may be, to have recourse to any such law or suit, notwithstanding that the tax is being recovered from the assessee by any mode specified herein before.



STUDY NOTE - 22

DEDUCTION AND COLLECTION OF TAX AT SOURCE

This Study Note includes

- Provisions relating to TDS
- Provisions relating to TCS

22.1 DEDUCTION OF TAX AT SOURCE (TDS)

LIABILITY FOR TDS

Any person responsible for making payment of certain category of incomes is liable to deduct tax at source at an appropriate occasion.

The law prescribes time when the TDS is to be made, rate at which it should be made, when TDS should be paid to the Government and associated administrative responsibilities of payer (tax deductor) and payee (tax deductee) have been prescribed.

The following chart states at a glance incomes from which TDS should be made :

Section	Nature of Income/ Payment	Threshold Limit	Person Responsible to Make TDS	Nature of payee	Rate at which to be deducted
192	Salary	Maximum amount not liable to tax for employee	Any person being an Employer	Employee having taxable salary	average rate of income-tax computed on the basis of rates in force for the financial year in which the payment is made, on the estimated salary income of the employee for that financial year
193	Interest on securities	10,000	Any person issuing the security	Any person	Refer Note No. 1
194A	Any interest other than interest on securities exceeding	₹5,000 in a year or 10,000 in case of banking company or co-operative society or deposit with post office	Any person other than individual or HUF [Refer Note No. 4]	Any resident in India	Refer Note No. 1
194B	Winnings from lottery or crossword puzzle or card game and other game of any sort including television game	₹ 5,000	Any person	Any person	30% [Sec. 115BBB]

Section	Nature of Income/ Payment	Threshold Limit	Person Responsible to Make TDS	Nature of payee	Rate at which to be deducted
194BB	Winnings from horse race	₹ 2,500	Winning from horse race	Any person	30% [Sec. 115BBB]
194C(1)	Any Payment in pursuance of any	If a contract exceeds contract ₹ 20,000 or total in a year contracts with the same contractor exceed ₹ 50,000.	Central or State Government, Local Authority, Central/State or Provincial Corpn., Company Cooperative Society Housing Board, Trust or University, Firm [Refer Note No. 4]	Any resident contractor for carrying out any work including supply of labour	1% for Advertisement contracts and 2% for all other contracts.
194C(2)	Any Payment in pursuance of any contract for consideration	₹ 20,000	Any contractor other than Individual and HUF [Refer Note No. 4]	Any resident sub-contractor	1%
194D	Insurance commission	₹ 5,000	Any person	Any resident person	Refer Note No. 1
194E.	Income for (i) participation in any game or sport in India; (ii) by way of remuneration for articles on sports, etc	Nil	Any person	Any non-resident sportsman who is not a citizen of India	10%
194E.	Guaranteed sum in relation to any game or sport played in India.	Nil	Any person	Any non-resident association or institution.	Refer Note No. 1
194EE	Any sum out of National Savings Scheme u/s 80CCCA	₹ 2,500	Any person	Any person	20%
194F	Amount on account of re-purchase relevant of units covered u/s. 80CCB	Nil	Any person	Any person	20%

Section	Nature of Income/ Payment	Threshold Limit	Person Responsible to Make TDS	Nature of payee	Rate at which to be deducted
194G	Commission, remuneration or prize – relating to lottery tickets	₹ 1,000	Any person	Any person stocking, purchasing or selling lottery tickets.	10%
194H	Commission Any person or Brokerage	₹ 2,500	Other than individual and HUF [Refer Note No. 4]	Any person	10%
194-I	Rent	₹1,20,000	Other than individual and HUF [Refer Note No. 4]	Any person	10 % plant, equipment other assets –15% incl. HUF payee 20% other payees
194J	Fees for Professional or technical services	₹30,000	Other than individual & HUF [Refer Note No. 4]	Any person	10%
194LA	Immovable Property Acquisition Compensation.	₹1,00,000	Any person	Any resident person	10%
195	Any interest or any sum chargeable as income (other than salary)	Nil	Any person	Any non-resident other than company Any foreign company	Refer Note No. 1 and if the NR is resident of a country with which India has Double Tax Avoidance Agreement, (DTAA) beneficial of the rate as per FA or DTAA.
196B	Income in respect of units referred to in Sec. 115A purchased in foreign currency or income of long term capital gains from such units.		Any person	Off shore fund	10%

Notes :

1. Threshold Limit: payments in a year upto this limit are not liable for TDS. In the amount of payment exceeds threshold limit, then provisions of TDS apply.
2. Rate of TDS is prescribed by the Finance Act (FA) that is applicable during the year when TDS is to be made. For example, for the current year from 1st April, 2010 to 31st March, 2011 (2010-11) TDS rates will be available in the Finance Act, 2010.
3. TDS rates specified herein above are rates of income tax. These are required to be increased by surcharge, education cess, etc. specified in The Finance Act applicable.
4. Individual and HUF :

An individual or a Hindu undivided family, whose total sales, gross receipts or turnover from the business or profession carried on by him exceed the monetary limits specified under clause (a) or clause (b) of section 44AB during the financial year immediately preceding the financial year in which such income is credited or paid, shall be liable to deduct income-tax under this section

Payments made by way of fees which are exclusively for personal purposes will not attract provisions of sec. 194J.

Rationalisation of provisions relating to tax deduction at source (TDS) [W.e.f. 1-10 2009]

Tax deduction at source is a method of collecting taxes on behalf of the Government at the time of payment or credit. The Income-tax Act casts a legal responsibility on the deductor to deduct tax on the correct amount, at the correct rate and deposit it to the Government account. The TDS rates are specified partly in the Finance Act and partly in the provisions of the Income-tax Act. Deductors are also required to compute surcharge and cess over and above some of the prescribed rates of TDS. If the deductor fails to deduct the tax or fails to deposit the tax after deduction, interest, penalty and prosecution provisions may get attracted. Further, under the provisions of section 40(a)(a), if the deductor fails to deduct tax on a prescribed payment or fails to deposit the tax deducted in time, the entire expenditure is disallowed while computing his total income. To assist deductors in complying with their TDS obligations and reduce their compliance burden, it is proposed to rationalise the provisions of TDS as under:

(A) Amendment in TDS rates and other provisions of section 194C

- (i) **Rate of TDS under section 194C rationalized [W.e.f. 1-10-2009]:** Under the existing provisions of section 194C of the Income-tax Act, TDS at the rate of 2% is deducted on payment for a contract. However, in the case of a sub-contract, TDS is deducted at the rate of 1%. Further, in the case of payment for an advertising contract, TDS is required to be deducted at the rate of 1%.

In order to reduce the scope for disputes regarding classification of contract as sub contract, the Act has specified the same rate of TDS for payments to both contractors as well as sub-contractors. To rationalise the TDS rates and to remove multiple classifications the Act has provided same rate of TDS in the case of payment for advertising contracts. To avoid hardship to small contractors/sub-contractors most of whom are organized as individuals/HUFs, the Act has prescribed following rates of TDS:

- (a) 1% where payment for a contract are to individuals/HUF
- (b) 2% where payment for a contract are to any other entity.

The nil rate will be applicable if the transporter quotes his PAN. If PAN is not quoted the rate will be 1% for an individual/HUF transporter and 2% for other transporters up to 31.3.2010.

The rate of TDS will be 20% in all the above cases, if PAN is not quoted by the deductee w.e.f. 1-4-2010.

- (i) Provisions for payments and tax deducted at source to transporters [W.e.f. 1-10-2009] : Under section 194C, tax is required to be deducted on payments to transport contractors engaged in the business of plying, hiring or leasing goods carriages. However if they furnish a statement that they do not own more than two goods carriages, tax is not to be deducted at source. Transport operators report problem in obtaining TDS certificates as these are not issued immediately by clients and they are not able to approach the client again as they may have to move across the country for their business. The Act has inserted sub-section (6) to section 194C and has exempted payments to transport operators (as defined in section 44AE) from the purview of TDS. However, this would only apply in cases where the operator furnishes his Permanent Account Number (PAN) to the deductor. As per section 194(7), the deductors who make payments to transporters without deducting TDS (as they have quoted PAN) will be required to intimate these PAN details to the Income Tax Department in the prescribed format.
- (iii) Clarification regarding “work” under section 194C [W.e.f. 1-10-2009]: There is ongoing litigation as to whether TDS is deductible under section 194C on outsourcing contracts and whether outsourcing constitutes work or not. To bring clarity on this issue, the Act has provided that “work” shall not include manufacturing or supplying a product according to the requirement or specification of a customer by using raw material purchased from a person other than such customer ns such a contract is a contract for ‘sale’. This will however not apply to a contract, which does not entail manufacture or supply of an article or thing (e.g. a construction contract). The Act has included manufacturing or supplying a product according to the requirement or specification of a customer by using material purchased from such customer, within the definition of ‘work’. It is further provided in section 194C(3) that in such a case TDS shall be deducted on the invoice value excluding the value of material purchased from such customer if such value is mentioned separately in the



invoice. Where the material component has not been separately mentioned in the invoice, TDS shall be deducted on the whole of the invoice value.

There is no change in the limit of ₹ 20,000 and ₹ 50,000 which is applicable for non deduction of tax at source under section 194C. Further, in a case where the payment is made by an individual or HUF to the contractor exclusively for personal purposes of such individual or member of HUF, there will be no need to deduct tax at source under section 194C.

(B) Rate of TDS reduced in case of section 194-I [W.e.f. 1-10-2009] : Under the existing provisions of section 194-I of the Income-tax Act, TDS on rental payments is prescribed at the rate of—

- (a) 10% for the use of any machinery or plant or equipment,
- (b) 15% for the use of any land or building or furniture or fittings, if the payee is an individual or HUF, and
- (c) 20% if the payee is other than an individual or HUF.

The Act has rationalised and reduced the TDS rates on rental payments as under:

- (a) 2% for the use of any machinery or plant or equipment,
- (b) 10% for the use of any land or building or furniture or fittings for all persons.

Nature of Payment (19 4-I) - Rent		Rate upto 30-9-2009	New rate * (w.e.f. 1-10-2009)
(a)	Rent of plant, machinery of equipment	10%	2%
(b)	Rent of land, building or furniture to an individual and Hindu undivided family	15%	10%
(c)	Rent of land, building or furniture to a person other than an individual or Hindu undivided family	20%	10%

The rate of TDS will be 20% in all the above cases, if PAN is not quoted by the deductee w.e.f. 1-4-2010.

(C) Rate of TDS on unlisted debentures or security or on Interest other than securities reduced to 10%.

Rate of TDS has been reduced by the Finance (No. 2) Act, 2009 from 20% to 10% in case of the following :

- (i) TDS on interest on unlisted debentures and on any income other than mentioned in Para 1(o) of Part II of Schedule I to the Finance (No. 2) Act, 2009 relating to TDS rates in case of a person other than a company who is resident in India has been reduced from 20% to 10%.
- (ii) Similarly, TDS on interest other than interest on securities and on any income other than mentioned in Para 2(a) of Part II of the Schedule I to the Finance (No. 2) Act, 2009 in case of a domestic company has also been reduced from 20% to 10%.

(D) TDS to be deducted at basic rates

In order to ease the computation of TDS, the Act has removed surcharge and education cess & SHEC on tax deducted on any payment made to resident taxpayers except in case of salary. In case of salary TDS shall be deductible after including education cess and SHEC. This provision shall be effective after the Finance (No. 2) Act becomes the Act.

(E) Section 197A has been amended : relating to tax benefits for new pension system extended to “Self Employed” u/s 10(44), 115-O and 80CCD [w.r.e.f. AY 2009-10]

Case Law :

(i) The directors of the assessee company have routed the loan taken in their individual capacity in the name of company. The company was merely acting as the agent of the directors for receiving & disbursing the loans to the directors. It was held that as per the provisions of section 194A, TDS is to be made at the time of credit of such income to the account of the payee. So the company was liable to deduct tax on the interest payment to lenders as there was no resolution passed by the Board of Directors which empowered the company to merely act as a medium for routing the borrowing & repayment. CIT v Century Building Industries P. Ltd. 293 ITR 194.

(ii) The assessee has entered into an agreement for use of the premise for storage of goods. While making payment the assessee deducted tax at 2% u/s 194C considering that it was a contractual payment. However it was concluded that the payment made by the assessee is in the nature of rent u/s 194I of the Act & TDS should have been made @20%. The Apex court held that once tax is paid by the deductee on the income received from the deductor, the deductor cannot be once again called upon to pay the tax on same income. However the assessee is liable to pay interest u/s 201(1A) for delay or non-payment of tax to the Government within prescribed time. Hindustan Coca Cola Beverages P. Ltd. v CIT 293 ITR 226 (SC).

IMPORTANT POINTS

1. Time Schedule

Nature of Activity		Time Frame
Time of Deduction		Salary : At the time of payment Others : When income paid or credited to the account including “payable” or “suspense” account whichever is earlier.
Time of deposit of tax (Other than on behalf of Government)		(a) If credited on the date on which accounts are made, within two months from the end of the month in which income is credited.
		(b) Any other case, within one week from the end of the month in which deduction is made.
Statement		For each Quarter
TDS Type	Form	For all category of Statements
Salary	No 24Q	Q1 : April – June – 15 th July
Non Resident	No 26Q	Q2 : July – September – 15 th October
All Others	No 27Q	Q3 : October – December – 15 th January
		Q4 : January - March - 15 th June
Electronic For		every office of Government and the principal officer in the case of every company, firm, whose total sales, gross receipts or turnover from the business or profession carried on by it exceed the monetary limits specified under clause (a) or clause (b) of section 44AB during the financial year immediately preceding the financial year in which such income is credited or paid.

- Copies of Form Nos. 15G and 15H received by the payer have to be filed with the Chief Commissioner within 7 days of the succeeding month.
- If the person responsible for deducting and paying tax fails to do so, he shall be considered as an assessee in default, liable to pay interest @ 12% p.a. on the amount of such tax from the date on which such tax was deductible to the date of actual payment, and penalty, not exceeding the amount of tax and rigorous imprisonment ranging from 3 months to 7 years and fine. The interest payment needs to be paid before filing of Quarterly Return.
- Sec. 199 – Credit for tax deducted :
 - Credit will be given for the assessment year in which such income is assessable.
 - Where such income is assessable in the hands of any other person, credit shall be given to such other person.
 - When any security, property etc. is jointly owned by two or more persons not constituting partnership, credit for TDS on income there from shall be given to such persons in the proportion in which the income is distributed.



4. A payee from whose income TDS is made must intimate his PAN to tax deductor. Tax deductor must to quote PAN of payees in TDS Certificate and TDS return [Sec. 139A].
5. TAN/TDCAN to be quoted on all quarterly statements of TDS/ TCS section 203A(ba).
6. A declaration for non-deduction of tax u/s. 197A can be furnished by the assessee only if his aggregate income is less than threshold limit. Senior Citizens can file declaration if tax on their estimated total income is likely to be NIL.

7. Disallowance due to non-deduction:

If tax deductible u/ ss. 193, 194A, 194C, 194H, 194J and 195 is not deducted/paid before applicable due dates, the relevant expenditure otherwise allowable in computing Total Income of the payer would be liable for disallowance u/s 40(a)(i)/(ia). The deduction will be allowed in the year in which TDS is paid. For details see section 40(a).

8. Salary TDS:

TDS by Employer : In respect of any perquisite which is not provided for by way of monetary payment, the Employer, at his option, may pay tax on the whole or part of such income without making any deduction there from. For the purpose of paying tax as aforesaid, tax shall be determined at the average of income-tax computed on the basis of the rates in force for the financial year, on the income chargeable under the head "Salaries".

Simultaneous employment / Successive employment : the employee may furnish to one of the many or successive employers such details of the income under the head "Salaries" due or received by him from the other employer or employers, the tax deducted at source there from and such other particulars and thereupon such employer shall take into account the details so furnished for the purposes of making the TDS

Relief Under Section 89(1) : Government servant or an employee in a company, co-operative society, local authority, university, institution, association or body is entitled to the relief under section 89(1), he may furnish to the employer, such particulars and thereupon the said Employer shall compute the relief and take it into account in making the TDS.

Other Income: Employee has any income chargeable under any other head of income for the same financial year, not being a loss under any such head other than the loss under the head "Income from house property", he may send to the Employer the particulars of—

- (a) such other income and of any tax deducted thereon under any other provision of this Chapter;
- (b) the loss, if any, under the head "Income from house property", and thereupon the Employer shall take—
 - (i) such other income and tax, if any, deducted thereon; and
 - (ii) the loss, if any, under the head "Income from house property",

also into account for the purposes of making the TDS:

After considering such other information there should be no reduction in TDS from Salary, except reduction on account of loss from "House Property" head.

PF, Superannuation Trusts : The trustees the fund at the time an accumulated balance due to an employee is paid, make there from the deduction provided in rules

Salary payable in foreign currency: Value in rupees of such salary shall be calculated at the prescribed rate of exchange.

9. **Income payable "net of tax":** In a case where, the tax chargeable on any income referred subject to TDS, the amount of TDS is to be borne by the person by whom the income is payable, then, for the purposes of deduction of tax under those provisions such income shall be increased to such amount as would, after deduction of tax thereon at the rates in force for the financial year in which such income is payable, be equal to the net amount payable under such agreement or arrangement. [Sec. 195A]

Procedure for TDS

- (i) To obtain Tax Deduction and Collection Account Number (TAN) by applying in Form No. 49B [sec. 203A and Rule 114A]
- (ii) To deduct tax at source as per provisions. TDS should be at an appropriate time and at appropriate rate.
- (iii) To deposit tax in the Government treasury within the time in proper challan
- (iv) To submit quarterly TDS statements.

Consequence of non compliance of TDS provisions :

Sr. No.		Section	Default	Consequence
			Section	Effect
1	197A	Delay, no submission of no TDS declarations	272A(2)(j)	₹ 100 per day / Max. Tax Amount on Declaration
2	Chapter XVII - B	Fails to deduct the whole or any part of TDS	271C(1)(a)	Penalty of a sum equal to the amount of TDS not so deducted. (ii) Fails to deduct the whole or any part of TDS: Penalty :- a sum equal to the amount of TDS not so deducted. [sec. 271C(1)(a)]
3	200	Delay in payment of TDS	201(1A)	Interest @ 1% p.m
4	200	Delay, no submission of Quarterly TDS Statement	272A(2)(k)	₹ 100 per day / Max. Tax Amount of TDS in of Quarterly TDS Statement
5	203A	Default in the matter of TAN	272BB	Penalty ₹ 10,000

Improving compliance with provisions of quoting PAN through the TDS regime [Section 206AAJ [W.e.f. 1-4 2010]

In order to strengthen the PAN mechanism, the Act has made amendments in the Income Tax Act to provide that any person whose receipts are subject to deduction of tax at source i.e. the deductee, shall mandatory furnish his PAN to the deductor failing which the deductor shall deduct tax at source at higher of the following rates :

- (i) The rate prescribed in the Act;
- (ii) At the rate in force i.e., the rate mentioned in the Finance Act; or
- (iii) At the rate of 20%.

TDS would be deductible at the above-mentioned rates even in a case where the taxpayer files a declaration in form 15G or 15H (under section 197A) but does not provide his PAN. Further, no certificate under section 197 will be granted by the Assessing Officer unless the application contains the PAN of the applicant.

These provisions will also apply to non residents where TDS is deductible on payments or credits made to them. To ensure that the deductor knows about the correct PAN of the deductee it is also provided for mandatory quoting of PAN of the deductee by both the deductor and the deductee in all **correspondence**, bills and vouchers exchanged between them.

Processing of statements of tax deducted at source (Section 200A inserted w.e.f. 1-4-2010)

Currently almost all statements of tax deducted at source are filed in an electronic mode. The processing of these statements should, therefore, be done only in a computerized environment.



New section 200A has been inserted provide for processing of statements of tax deducted at source on computer so that liabilities on account of interest and other defaults in TDS payment are promptly calculated and intimated to the deductor. In order to process TDS statements on computer, the Act has provided for electronic processing on the same lines as processing of Income-tax returns.

Further, the following adjustments can be made during the computerized processing of statements of tax deducted at source :

- (i) Any arithmetical error in the statement; or
- (ii) An incorrect claim, if such incorrect claim is apparent from any information in the statement, for example, in respect of rate of deduction of tax at source where such rate is not in accordance with the provisions of the Act.

The Act has provided that after making adjustments, tax and interest [e.g. under section 201(1A)] would be calculated and sum payable by the deductor or refund due to the deductor will be determined. An intimation will be sent to the deductor informing him of his tax liability or granting him the refund due within one year from the end of the financial year in which the statement is filed. The Act has also provided that the processing of these statements can be undertaken in a centralized processing centre.

Providing time limits for passing of orders under section 201(1) holding a person to be an assessee in default

Currently, the Income Tax Act does not provide for any limitation of time for passing an order under section 201(1) holding a person to be an assessee in default. In the absence of such a time limit, disputes arise when these proceedings are taken up or completed after substantial time has elapsed.

In order to bring certainty on this issue, the Act has inserted sub-section (3) to section 201 to provide for express time limits in the Act within which specified order under section 201(1) will be passed.

An order under section 201(1) passed on or after 1-4-2010, for failure to deduct the whole or any part of the tax as required under this Act, if the deductee is a resident taxpayer shall be passed within two years from the end of the financial year in which the statement of tax deduction at source is filed by the deductor.

Where no such statement is filed, such order can be passed up till four years from the end of the financial year in which the payment is made or credit is given.

Further, Explanation\ to section 153 regarding exclusion of certain period (like injunction by Court) to calculate time limit shall also be applicable while determining the above time limit. Similarly like section 153(3) there will be no time limit in consequence of or to give effect to any finding or direction contained in an order under section 250, 254, 260A, 262, 263 or 264 or order of a Court. To provide sufficient time for pending cases, the Act has provided that such proceedings for a financial year beginning from 1-4-2007 and earlier years can be completed by the 31-3-2011.

However, no time-limits have been prescribed for order under section 201(1) where—

- (a) The deductor has deducted but not deposited the tax deducted at source, as this would be a case of defalcation of government dues,
- (b) The employer has failed to pay the tax wholly or partly, under section 192(1A), as the employee would not have paid tax on such perquisites
- (c) The deductee is a non-resident as it may not be administratively possible to recover the tax from the non-resident.

These amendments shall be effective from 1-4-2010. Accordingly it will apply to such orders passed on or after the 1-4-2010.

22.2 TAX COLLECTION AT SOURCE [Sec. 206C]

Every seller at the time of debiting the buyer with the amount payable or receiving payments from buyers engaged in business of alcoholic liquor, forest produce, scrap, timber, tendu leaves, etc. shall collect tax at the following rates:

Sr.No	Nature of goods	TCS Rate
1	Alcoholic liquor for human consumption (other than Indian made foreign liquor)	1%
2	Tendu leaves	5%
3	Timber obtained under a forest lease	2.5%
4	Timber obtained by any mode other than under a forest lease	2.5%
5	Any other forest produce not being timber or tendu leaves	2.5%
6	Scrap	1%

Every person, who grants a lease or a license or enters into a contract, etc for the purpose mentioned below shall collect tax at the following rates:

TABLE

Sl. No.	Nature of contract or licence or lease, etc.	TCS Rate
(i)	Parking lot	2%
(ii)	Toll plaza	2%
(iii)	Mining and quarrying	2%

The amount of tax so collected shall be paid, within one week seven from end of the month of tax collection. Delay or failure attracts interest @ 1% p.m. [sec. 206C(7) & (8)]

Responsibility & Liability of the Tax Collector

1. To obtain Tax Collection Account No. [sec. 206CA(1)]
2. To quote TCS No. in all returns, certificates and challans. [sec. 206CA(2)]
3. To furnish quarterly return in form No. 27EQ within stipulated time i.e. within fifteen days from the end of a quarter for the first three quarters and by 30th April for the last quarter.
4. Failure to furnish TCS return: Penalty @ 100/- per day, during which the default continues, but not exceeding the amount of TCS. [sec. 272A(2)(g)]
5. Failure to deposit TCS in Government treasury, rigorous imprisonment for a term of not less than 3 months, but which may extend to 7 years, in addition to fine [secs. 276B & 276BB]

Thus, administrative provisions are similar to TDS administration.

Filing of TDS and TCS statements (W.e.f. 1-10-2009)

Section 200(3) of Income-tax Act provides that any person deducting tax in accordance with the provisions of Chapter XVII B has to furnish, within the prescribed time, quarterly statements for the period ending on the 30th June, 30th September, 31st December and 31st March in each financial year. Similarly, filing of quarterly returns for tax collection at source (TCS) have been provided in sub-section (3) of section 206C of the Act. Further section 206A provides furnishing of quarterly return in respect of payment of interest to residents without deduction of tax.

In order to provide administrative flexibility in deciding the periodicity of such TDS related statements, the Act has modified the existing provisions so as to allow the Government to prescribe periodicity of such TDS statements besides prescribing their form and manner.

Further, section 272A(2)(0) relating to non-filing of quarterly statement of TDS/TCS has been amended in order to delete the word 'quarterly' given for such statements.



STUDY NOTE - 23

PENALTIES & PROSECUTION

This Study Note includes

- Different Defaults and Penalties related thereto

PENALTIES

Section	Nature of Default	Minimum Penalty	Maximum Penalty
158BFA	Undisclosed income determined by the Assessing Officer u/s.158BC(c)	100% of the tax on undisclosed income	300% of the tax on undisclosed income.
221(1)	Default in making a payment of tax within prescribed time	Such amount as the Assessing Officer may impose	Tax in arrears
271(1)(b)	Failure to comply with a notice u/s. 142(1) or 143(2) or with a direction issued u/s.142(2A).	₹10000 for each failure	₹ 25,000 for each failure.(upto 31.5.2001)
271(1)(c)	Concealment of the particulars of income or furnishing inaccurate particulars of income.	100% of Tax sought to be evaded.	300% of Tax sought to be evaded.
271A	Failure to keep or maintain books of A/c, document as required u/s.44AA.	₹25000	₹1,00,000
271AA	Failure to keep and maintain information and document in respect of international transaction.	a sum equal to two per cent of the value of each international transaction entered into by such person.	a sum equal to two per cent of the value of each international transaction entered
271AAA	Penalty where search has been initiated	a sum computed at the rate of ten per cent of the undisclosed income of the specified previous year.	a sum computed at the rate of ten per cent of the undisclosed income of the specified previous year.
271B	Failure to get accounts audited u/s.44AB or to furnish such report along with return of income by due date.	1/2% of Total Sales, Turnover or Gross receipts.	₹1,00,000
271C	Failure to deduct the whole or any part of tax u/s.192 to 195 or (w.e.f. 1.6.97) failure to pay the whole or any part of tax u/s.115 O(2) or 2nd proviso to sec. 194B.	Amount of Tax required to be deducted at source.	—

Section	Nature of Default	Minimum Penalty	Maximum Penalty
271CA	Penalty for failure to collect tax at source	a sum equal to the amount of tax	a sum equal to the amount of tax
271D	Taking or accepting any loan or deposit in contravention of the provisions of Sec.269 SS Repaying of any deposit otherwise than in accordance with the provisions of Sec. 269 T	Amt. of Loan/Deposit so taken or accepted Amount of deposit so repaid.	— —
271F	(i) Failure to furnish return of income u/s.139(1) before the end of the relevant assessment year(w.e.f. 1.4.99) (ii) Failure to furnish return of income as per proviso to Sec.139(1) by the end of relevant assessment year.	₹ 5000 ₹ 5000 for each default.	— ₹ 10,000 for each default
271FB	Penalty for failure to furnish return of fringe benefits	a sum of one hundred rupees for every day during which the failure continues.	a sum of one hundred rupees for every day during which the failure continues.
272A(1)(a)	Refuses to answer any question put to a person regarding his assessment by an I.T. Authority.	₹10,000 for each default	₹ 10,000 for each default
272A(1)(b)	Refuses to sign any statement made by a person in course of I.T. Proceeding.	₹10,000 for each default	₹ 10,000 for each default
272A(1)(c)	Failure to comply with summons issued u/s.131(1)	₹10,000 for each default	₹ 10,000 for each default
272AA	Failure to comply with provisions of Sec. 133B.	Any amount upto	₹ 1000
272B	Failure to comply with the provisions of section 139A or for quoting or intimating a PAN which is false. [w.e.f. 1.6.2002]	₹ 10,000	₹ 10,000
272BB	Failure to comply with the provisions of section 203A (i.e. failure to obtain TAN or after obtaining failure to quote TAN in all challans, certificates and returns etc.)	₹ 10,000	₹ 10,000
272BBB	Failure to comply with the provisions of of sec. 206CA (i.e failure to obtain TCAN or after obtaining failure to quote TCAN in all challans, certificates and returns etc.) (w.e.f. 1.6.2002)	₹ 10,000	₹ 10,000
276C(1)	Wilful attempt to evade tax penalty or interest imposable under the Act (non-cognizable as per sec. 279A)	If tax evaded exceeds ₹ 1,000, 6 months; otherwise 3 months and fine.	If tax evaded exceeds ₹ 1,00,000, 7 years; otherwise 3 years and fine.
276C(2)	Wilful attempt to evade the payment of any tax, penalty or interest (non-cognizable as per sec. 279A).	3 months and fine	3 years and fine

Section	Nature of Default	Minimum Penalty	Maximum Penalty
276CC	Wilful failure to file return of income in time u/s. 139(1), or in response to notice u/s. 142(1) or sec. 148(Non-cognizable as per sec. 279A)	If tax evaded exceeds ₹ 1,00,000; 6 months and fine In any other case, 3 months and fine. Note: No prosecution if : (i) the return is filed before the expiry of the assessment year ; or (ii) the tax payable on regular assessment, as reduced by TDS and advance tax does not exceed ₹ 3,000	If tax evaded exceeds ₹ 1,00,000, 7 years; otherwise 3 years and fine
276CCC	Wilful failure to furnish in due time the return of total income which is required to be furnished u/s. 158BC.	3 months and fine	3 months and fine
276D	Wilful failure to produce books of account and documents u/s. 142(1) or wilful failure to comply with a direction to get the accounts audited u/s. 142(2A)	Any period upto 1 year and fine of ₹ 4 for every day during which default continues.	1 year and fine of ₹ 10 every day during which default continues.

Rationalisation of provisions relating to penalty for concealment of income in the course of search {Explanation 5A to section 271(1) | [W.r.e.f. 1-6-2007]}

Under the existing provisions of Explanation 5A to sub-section (I) of section 271, it has been provided that where, in the course of search initiated under section 132 on or after 1-6-2007, the assessee is found to be owner of—(i) any money, bullion, jewellery or other valuable article or thing (hereinafter referred to as assets) and the assessee claims that such assets have been acquired by him by utilizing (wholly or in part) his income for any previous year; or (ii) any income based on any entry in any books of account or other documents or transactions and claims that such assets or entry in the books of account or other documents or transactions represents his income (wholly or in part) for any previous year; which has ended before the date of the search and the due date for filing the return of income for year has expired and the assessee has not filed the return, then, notwithstanding that such income is declared by him in any return of income furnished on or after the date of the search, he shall, for the purposes of imposition of a penalty under clause (c) of sub-section (1) of this section, be deemed to have concealed the particulars of his income or furnished inaccurate particulars of such income.

In order to clarify that the scope of Explanation 5 A also extends to cases where the assessee has filed the return of income for any previous year and the income found during the course of search relates to such previous year and is not disclosed in the said return, then such income shall be deemed to be concealed income and assessee shall be liable to pay penalty under section 271. Therefore, the Act has substituted the Explanation 5A to sub-section (1) of section 271 so as to provide that where in the course of a search initiated under section 132 on or after 1-6-2007, the assessee is found to be the owner of—

- (i) Any money, bullion, jewellery or other valuable article or thing (hereinafter referred to as assets) and the assessee claims that such assets have been acquired by him by utilizing (wholly or in part) his income for any previous year; or
- (ii) Any income based on any entry in any books of account or other documents or transactions and he claims that such entry in the books of account or other documents or transactions represents his income (wholly or in part) for any previous year, which has ended before the date of search and,
- (a) **Where the return of income for such previous year has been furnished before the said date but such income has not been declared therein; or**
- (b) The due date for filing the return of income for such previous year has expired but the assessee has not filed the return, then, notwithstanding that such income is declared by him in any return of income furnished on or after the date of the search, he shall, for the purposes of imposition of a penalty under clause (c) of sub-section (1) of this section, be **deemed to have coin-titled the particulars of his income or furnished inaccurate particulars of such income.**

Case Laws:

Section	Case Laws
221	<ul style="list-style-type: none"> (i) Burden is on Revenue: In the matter of penalty, read with section 201, an obligation is cast upon the Assessing Officer to be satisfied that default by assessee was without good and sufficient reason. The burden is upon the revenue to establish that the assessee has not deposited the tax at source without good and sufficient reasons. In other words, in absence of such finding, no negative terms for levying penalty can be made and the burden specifically lies on the revenue - <i>CIT v. Munni Lal & Co.</i> 157 Taxman 466 (ii) Penalty is attracted the moment default has occurred - An assessee incurs a liability to penalty the moment default has occurred, notwithstanding the fact the default has ceased to exist by the time the authorities concerned take action to penalise the assessee for the said default - <i>CIT v. Smt. Vijayanthimala</i>
271C	<ul style="list-style-type: none"> (i) Levy of penalty is attracted only if there is no reasonable cause - Levy of penalty under section 271C is not automatic. Before levying penalty, the concerned officer is required to find out that even if there was any failure referred to in the concerned provision the same was without a reasonable cause. The initial burden is on the assessee to show that there existed reasonable cause which was the reason for the failure referred to in the concerned provision. Thereafter the officer dealing with the matter has to consider the explanation offered by the assessee or the person, as the case may be. 'Reasonable cause' as applied to human action is that which would constrain a person of average intelligence and ordinary prudence. It can be described as probable cause. It means an honest belief founded upon reasonable grounds, of the existence of a state of circumstances, which assuming them to be true, would reasonably lead any ordinary prudent and cautious man, placed in the position of the person concerned, to come to the conclusion that the same was the right thing to do. The cause shown has to be considered and only if it found to be frivolous, without substance or foundation, the prescribed consequences follow - <i>Woodward Governor India (P) Ltd. v. CIT</i> 253 ITR 745
271(1)(c)	The Supreme court in this case held that in force from 1 st April 2003, there cannot be liability to penalty when there is no liability to tax especially because penalty has to be worked out with reference to the tax payable as contrasted with the income concealed. <i>Virtual Soft Systems ltd vs CIT</i> 289 ITR 83(SC).
272A	<ul style="list-style-type: none"> (i) If penalty has been levied under section 271C for failure to deduct tax at source, question of levying penalty under section 272A(2)(c) and 272A(2)(g) would also not arise - Once a person prescribed or concerned or the assessee has been subjected to a penalty under section 271C, for not deducting the tax at source, there would not arise any occasion for levying a penalty under section 272A(2)(c) and 272A(2)(g) for non-compliance of the provisions of sections 203 and 206. In other words, in case the tax has not been deducted at source, the question of issuing the certificate of tax under section 203 or that of filing of return under section 206 would not arise at all. That being so, the question of imposing penalty for violation of the aforesaid provisions, would also not arise - <i>CIT v. Sri Ram Memorial Education Promotion Society</i> 150 Taxman 58

Section	Case Laws
276B	<p>(i) Delayed payments are also covered - The wording of section 276B does not afford scope for treating the words 'fails to pay' as confined only to those cases where there is a total failure to pay the tax and not having application to those cases where there has been failure to pay within the prescribed time - <i>Rayala Corporation (P.) Ltd. v. V.M. Muthuramalingam</i>, ITO 129 ITR 675 ii) Merely because tax has been deposited to the credit of the Central Government before filing of the complaint, it will not absolve the assessee of the offence under section 276B - <i>Rishikesh Balkishandas v. I.D. Manchanda</i>, ITO 167 ITR 49 iii) Mens rea is not essential - Section 276B does not contain the word 'knowingly'. Therefore, in a case under section 276B, read with section 194A, mens rea is not required - <i>Rishikesh Balkishandas v. I.D. Manchanda</i>, ITO / Dy. CIT v. <i>Modern Motor Works</i> 87 Taxman 182/220 ITR 415</p>
276C	<p>(i) Company, whether can be prosecuted- A company cannot be prosecuted for offences under sections 276C, 277 and 278, since each one of these sections requires imposition of a mandatory term of imprisonment coupled with a fine and leaves no choice to Court to impose only a fine - <i>Asstt. Commissioner v. Velliappa Textiles Ltd.</i> 132 Taxman 165/263 ITR 550.</p> <p>(ii) Though a company cannot be sentenced to imprisonment, for that reason only company cannot be given complete immunity from prosecution for graver offences where mandatory punishment is imprisonment coupled with fine; Court has to resort to punishment of imposition of fine which is also a prescribed punishment - <i>Standard Chartered Bank v. Directorate of Enforcement</i> 145 Taxman 154/275 ITR 81.</p> <p>(iii) Mens rea must be present - To bring an act under the provisions of section 276C, the action of the person concerned has to be a wilful attempt to evade any tax, penalty or interest chargeable or impossible under the Act. The word 'wilful' imparts the concept of <i>mens rea</i>, and if <i>mens rea</i> is absent, no offence under this section is made out - <i>Jarnail Singh v. ITO</i> 179 ITR 426 /CIT v. <i>Gangaram Chapolia</i> 103 ITR 613 iv) If accused makes a full and complete disclosure, then prosecution under section 276C/277 should not be proceed - If accused makes a full and complete disclosure to get benefit of pardon under section 306 of the Code of Criminal Procedure, 1973, prosecution under section 276C/277 should not be allowed to proceed - <i>Dipesh Chandak v. Union of India</i> 270 ITR 85/140 Taxman 166.</p>
276CC	<p>(i) Mens rea is not an essential requirement - If section 276CC is read in isolation, the <i>mens rea</i> is an essential requirement of law and it would be for the prosecution to lead evidence to prove that the return was wilfully filed late. However, it is not so. Section 278E provides that in any prosecution for the offence under this Act which requires 'culpable mental state' on the part of the accused, the Court shall presume the existence of such mental state. The burden is shifted to the accused that he had no such mental state. As per the <i>Explanation</i>, the culpable state would include 'intention', 'motive' and 'knowledge'. It further provides that the absence of such culpable mental state shall have to be proved by the accused in defence beyond reasonable doubt. The Act does not differentiate in any way between natural and juristic persons. As per the settled law, charge can be framed even on the basis of strong suspicion - <i>V.P. Punj v. Asstt. CIT</i> 119 Taxman 543</p> <p>(ii) Whether there is wilful failure to furnish return is a matter which is to be adjudicated factually by the Court which deals with the prosecution case. Section 278E is relevant for this purpose. There is a statutory presumption prescribed in section 278E. The Court has to presume the existence of culpable mental state, and absence of such mental state can be pleaded by an accused as a defence in respect to the act of charged as an offence in the prosecution - <i>Prakash Nath Khanna v. CIT</i> 135 Taxman 327/266 ITR 1.</p> <p>(iii) Filing of voluntary return under section 139(4) will not absolve assessee from infraction of not filing return in time - One of the significant terms used in section 276CC is 'in due time'. The time within which the return is to be furnished is indicated only in section 139(1) and not in section 139(4). That being so, even if a return is filed in terms of section 139(4), that would not dilute the infraction in not furnishing the return in due time as prescribed under section 139(1). Otherwise, the use of the expression 'in due time' would lose its relevance and it cannot be said</p>

Section	Case Laws
Contd. 276C	that the said expression was used without any purpose. A person who had not filed a return within the due time as prescribed under sub-section (1) or (2) of section 139 would otherwise, get benefit by filing the return under section 139(4) much later. This cannot certainly be the legislative intent. Sub-section (4) of section 139 cannot by any stretch of imagination control operation of sub-section (1) wherein a fixed period for furnishing the return is stipulated - <i>Prakash Nath Khanna v. CIT</i> 135 Taxman 327.
276DD	(i) <i>Effect of omission of section</i> - Prosecution under section 276DD could not have been launched or continued by invoking section 6 of General Clauses Act after omission of section 276DD with effect from 1-4-1989 - <i>General Finance Co. v. Asstt. CIT</i> 257 ITR 338/124 Taxman 432.
278B	<p>(i) Meaning of 'person in charge' - A person in charge must mean that the person should be in overall control of the day-to-day business of the firm - <i>State of Karnataka v. Pratap Chand</i> 128 ITR 573.</p> <p>(ii) A plain reading of section 278B goes to show that it is for the prosecution in the first instance to demonstrate by averments and proof that the person was in charge of and was responsible to the company for the conduct of the business of the company. Therefore, while the company may be deemed to be guilty of the offence, so far as the partners or directors are concerned, only those persons can be prosecuted who are in charge of and responsible to the company for the conduct of its business - <i>Smt. Sitaben v. Union of India</i> 120 CTR (MP) 444.</p>



STUDY NOTE - 24

REFUND

This Study Note includes

- Provisions of the Income Tax Act relating to refund of taxes in the event of the tax paid being in excess of the tax liability

WHEN RIGHT TO CLAIM REFUND ARISES [Sec. 237]

Where any person satisfies the Assessing Officer that the amount of tax paid by him or on his behalf for any assessment year exceeds the amount with which he is properly chargeable under this Act for that year, he is entitled to the refund of the excess amount paid.

Case Law :

- (i) The tax paid by the assessee must be accepted as it is, and in the event of the tax paid being in excess of the tax liability duly computed on the basis of return furnished and the rates applicable, the excess shall be refunded to the assessee, since its retention may offend article 265 of the Constitution - *CIT v. Shelly Products* 261 ITR 367.

WHO CAN CLAIM REFUND ? [Sec. 238]

Usually refund can be claimed by a person who has made excess payment of tax. If income of a person is included in the total income of another person u/s. 60 to 64, the refund can be claimed by the latter and not by the former. Where a person cannot claim any refund because of his death, incapacity, insolvency, liquidation or other cause, his legal representatives or the trustee or guardian or receiver, as the case may be, will be entitled to claim and receive such refund for the benefit of such person or his estate.

Where the value of fringe benefits provided or deemed to have been provided by one employer is included under any provisions of Chapter XII-H in the value of fringe benefits provided or deemed to have been provided by any other employer, the latter alone shall be entitled to a refund under this Chapter in respect of such fringe benefits."

HOW TO CLAIM REFUND [Sec. 239]

Refund claim should be made in Form No. 30 and verified in the prescribed manner.

In the following cases, where an otherwise valid refund claim u/s. 237 is filed by an assessee after the expiry of the time limit, the Assessing Officer, may admit the refund claim if the following conditions are satisfied-

1. The refund arising as a result of tax deducted at source in respect of the assessment year under the provisions of section 192, 193, 194, 194A, 194B, 194C, 194D and 195 does not exceed ` 10,000;
2. the income returned is not a loss where the assessee claims the benefit of carry forward of the loss;
3. the refund claim is not supplementary in nature; and
4. the amount of the assessee is not assessable in the hands of any other person under any provisions of the Act.

Moreover, the A.O. is authorised to admit belated return claims upto ` 10,000 where the following conditions are satisfied –

- (i) the refund arising as a result of excess advance tax payment in respect of assessment year under the provisions of sec. 208, does not exceed ` 10,000;

- (ii) the returned income is not a loss, where the assessee claims the benefit of carry forward of the loss;
- (iii) the refund claimed is not supplementary in nature, i.e. a claim for additional amount of refund after the completion of the original assessment for the same assessment year ; and
- (iv) the income of the assessee is not assessable in the hands of any other person under section any provisions of the Act.

Case Law :

- (i) Board is competent to admit an application for refund even after expiry of period prescribed under section 239, for avoiding genuine hardship in any case or class of cases. *Union of India v. Azadi Bachao Andolan* 263 ITR 706.

REFUND ON APPEAL [Sec. 240]

- iii) Assessee is entitled to interest if the interest is paid u/s 220(2) subsequently becomes refundable: Interest u/s 244A is payable in respect of the amount of interest earlier paid by the assessee u/s 220(2) but later determined as refundable. *Modipon Ltd. V CIT* 270 ITR 257.

Case Laws :

- (i) Revenue is liable to pay interest on the amount of interest which it should have paid to the assessee but has unjustifiably failed to do - *CIT v. Narendra Doshi* 254 ITR 606/122 Taxman 717.
- (ii) Interest on delay payment of interest: The Department is liable to pay interest on interest under sections 214 and 244(1A) if payment of interest is delayed - *MC, Nally Bharat Engg. Co. Ltd. v. CIT* Tax L.R. 638
- (iii) Calculation of interest Interest cannot be granted till date of dispatch of refund order but it has to be granted till date when order regarding payment of interest has been signed - *Rajasthan State Electricity Board v. CIT* 281 ITR 274
- (iv) Where return is filed belatedly: Where delay in completion of assessment which led to refund was on account of delay in filing returns by assessee, assessee was not entitled to interest for period of said delay in terms of section 244A(2) - *M. Ahammadvkutty Haji v. Chief CIT* 155 Taxman 315

SET OFF OF REFUNDS AGAINST THE REMAINING PAYABLE [Sec. 245]

Where a refund is found to be due to any person, the tax authorities may, in lieu of payment of the refunds, set off the amount of refund against the sum payable under the Income-tax Act.

Case Law :

- (i) Prior intimation to assessee whether mandatory: While making set off of refunds against tax remaining payable, intimation is certainly not a jurisdictional requirement and absence thereof is merely an irregularity and, therefore, want of intimation would not vitiate the adjustment - *Brij Bhushan Lal & Sons v. Designated Authority* 246 ITR 353
- (ii) Refund due to assessee cannot be adjusted against demand raised, against a third party *Archana Shukla v. Joint CIT* 244 ITR 829.

Where refund arises as a result of any order passed in appeal or other proceedings under the Act, no formal application from the assessee is required. The AO has to grant refund suo moto.

Case Laws :

- (i) Clause (a) of proviso to section 240 added with effect from 1-4-1989 is merely clarificatory and hence, must be held to be retrospective - *CIT v. Chittoor Electric Supply Corpn.* 212 ITR 404 / *CIT v. Shelley Products* 261 ITR 367

Correctness of assessment not to be questioned [Sec. 242]

In a claim under this Chapter, it shall not be open to the assessee to question the correctness of any assessment or other matter decided which has become final and conclusive or ask for a review of the same, and the assessee shall not be entitled to any relief on such claim except refund of tax wrongly paid or paid in excess.



INTEREST ON DELAYED REFUNDS. [Sec. 243.]

[(1) If the [Assessing] Officer does not grant the refund,—

- (a) in any case where the total income of the assessee does not consist solely of income from interest on securities or dividends, within three months from the end of the month in which the total income is determined under this Act, and
- b) in any other case, within three months from the end of the month in which the claim for refund is made under this Chapter,

the Central Government shall pay the assessee simple interest at [fifteen] per cent per annum on the amount directed to be refunded from the date immediately following the expiry of the period of three months aforesaid to the date of the order granting the refund.

Explanation.—If the delay in granting the refund within the period of three months aforesaid is attributable to the assessee, whether wholly or in part, the period of the delay attributable to him shall be excluded from the period for which interest is payable.]

- (2) Where any question arises as to the period to be excluded for the purposes of calculation of interest under the provisions of this section, such question shall be determined by the [Chief Commissioner or Commissioner] whose decision shall be final.

[(3) The provisions of this section shall not apply in respect of any assessment for the assessment year commencing on the 1st day of April, 1989 or any subsequent assessment years.]

Interest on refund where no claim is needed [Sec. 244]

- (1) Where a refund is due to the assessee in pursuance of an order referred to in Section 240 and the [Assessing] Officer does not grant the refund within a period of [three months from the end of the month in which such order is passed], the Central Government shall pay to the assessee simple interest at [fifteen] per cent per annum on the amount of refund due from the date immediately following the expiry of the period of [three] months aforesaid to the date on which the refund is granted.

[(1A) Where the whole or any part of the refund referred to in sub-section (1) is due to the assessee, as a result of any amount having been paid by him after the 31st day of March, 1975, in pursuance of any order of assessment or penalty and such amount or any part thereof having been found in appeal or other proceeding under this Act to be in excess of the amount which such assessee is liable to pay as tax or penalty, as the case may be, under this Act, the Central Government shall pay to such assessee simple interest at the rate specified in sub-section (1) on the amount so found to be in excess from the date on which such amount was paid to the date on which the refund is granted :

Provided that where the amount so found to be in excess was paid in instalments, such interest shall be payable on the amount of each such instalment or any part of such instalment, which was in excess, from the date on which such instalment was paid to the date on which the refund is granted :

Provided further that no interest under this sub-section shall be payable for a period of one month from the date of the passing of the order in appeal or other proceeding :

Provided also that where any interest is payable to an assessee under this sub-section, no interest under sub-section (1) shall be payable to him in respect of the amount so found to be in excess.]

- (2) Where a refund is withheld under the provisions of Section 241, the Central Government shall pay interest at the aforesaid rate on the amount of refund ultimately determined to be due as a result of the appeal or further proceeding for the period commencing after the expiry of [three months from the end of the month in which the order referred to in Section 241 is passed] to the date the refund is granted.
- [(3) The provisions of this section shall not apply in respect of any assessment for the assessment year commencing on the 1st day of April, 1989, or any subsequent assessment years.]

INTEREST ON REFUND [Sec. 244A]

Interest on Refund of Income Tax: Where refund of any amount becomes due to the assessee under the Income Tax Act, he shall be entitled to receive, in addition to the said amount, simple interest on the refund calculated in the following manner:

- (a) Where the refund is out of any tax deducted at source/ tax collected at source or advance tax paid during the financial year, interest will be paid at the rate of $\frac{1}{2}\%$, per month or part of a month from the period starting from 1st day of April of the assessment year to the date on which refund is granted.
However, no interest shall be payable if the amount of refund is less than 10% of the tax determined u/s 143(1).
- (b) In other cases, interest shall be paid @ $\frac{1}{2}\%$ per month for every month or part of month for the period commencing from the date of payment of tax or penalty to the date on which refund is granted.

Interest on Refund of Fringe Benefit Tax: Section 244A also provides for interest @ $\frac{1}{2}\%$ for every month or part of the month shall be payable where refund of any amount out of fringe benefit tax paid by way of advance tax becomes due.

However, no interest shall be payable if the amount of refund is less than 10% of the tax determined u/s 115WE (1). Similarly interest @ $\frac{1}{2}\%$ for every month or part of month shall be payable in any other case for the period or periods from the date or dates of payment of tax or penalty to the date on which the refund is granted.

Judicial Decisions

- (i) Section 244(1) nowhere speaks of interest. Provisions of section 240 & 244 reveal liability to pay interest on delayed payment of refund amount but do not provide for payment of any interest on interest even though there is delay in payment of such interest to assessee. *Sandvik Asia Ltd. V CIT 280 ITR 643 (SC)*
- (ii) As the assessee has not received the refund of the excess advance tax, he preferred a writ petition before the Delhi High Court. When the writ petition was pending, the Department granted refund of advance tax along with interest thereon. The petitioner claimed interest on delayed payment of interest. The Delhi High Court held that the petitioner is entitled to interest on delayed payment of interest & accordingly directed the revenue to pay interest on interest. *R.K. Jain & Sons v CIT 193 CTR 659.*
- (iii) Assessee is entitled to interest if the interest is paid u/s 220(2) subsequently becomes refundable: Interest u/s 244A is payable in respect of the amount of interest earlier paid by the assessee u/s 220(2) but later determined as refundable. *Modipon Ltd. V CIT 270 ITR 257.*

Case Laws :

- (i) Revenue is liable to pay interest on the amount of interest which it should have paid to the assessee but has unjustifiably failed to do - *CIT v. Narendra Doshi 254 ITR 606/122 Taxman 717.*
- (ii) Interest on delayment payment of interest: The Department is liable to pay interest on interest under sections 214 and 244(1A) if payment of interest is delayed - *MC, Nally Bharat Engg. Co. Ltd. v. CIT Tax L.R. 638*
- (iii) Calculation of interest Interest cannot be granted till date of dispatch of refund order but it has to be granted till date when order regarding payment of interest has been signed - *Rajasthan State Electricity Board v. CIT 281 ITR 274*
- (iv) Where return is filled belatedly: Where delay in completion of assessment which led to refund was on account of delay in filing returns by assessee, assessee was not entitled to interest for period of said delay in terms of section 244A(2) - *M. Ahammadkutty Haji v. Chief CIT 155 Taxman 315*

SET OFF OF REFUNDS AGAINST THE REMAINING PAYABLE [Sec. 245]

Where a refund is found to be due to any person, the tax authorities may, in lieu of payment of the refunds, set off the amount of refund against the sum payable under the Income-tax Act.

Case Law :

- (i) Prior intimation to assessee whether mandatory: While making set off of refunds against tax remaining payable, intimation is certainly not a jurisdictional requirement and absence thereof is merely an irregularity and, therefore, want of intimation would not vitiate the adjustment - *Brij Bhushan Lal & Sons v. Designated Authority 246 ITR 353.*
- (ii) Refund due to assessee cannot be adjusted against demand raised, against a third party *Archana Shukla v. Joint CIT 244 ITR 829.*



STUDY NOTE - 25

SETTLEMENT OF CASES

This Study Note includes

- Provisions under the Income Tax Act relating to Settlement of Cases

SETTLEMENT OF CASES [SEC. 245A TO 245L]

INCOME-TAX SETTLEMENT COMMISSION [Sec. 245B]

- (1) The Central Government shall constitute a Commission to be called the Income-tax Settlement Commission for the settlement of cases under this Chapter.
- (2) The Settlement Commission shall consist of a Chairman [and as many Vice-Chairmen and other members as the Central Government thinks fit] and shall function within the Department of the Central Government dealing with direct taxes.
- (3) The Chairman [Vice-Chairman] and other members of the Settlement Commission shall be appointed by the Central Government from amongst persons of integrity and outstanding ability, having special knowledge of, and, experience in, problems relating to direct taxes and business accounts:

Provided that, where a member of the Board is appointed as the Chairman [Vice-Chairman] or as a member of the Settlement Commission, he shall cease to be a member of the Board.

JURISDICTION AND POWERS OF SETTLEMENT COMMISSION [Sec. 245BA]

- (1) Subject to the other provisions of this Chapter, the jurisdiction, powers and authority of the Settlement Commission may be exercised by Benches thereof.
- (2) Subject to the other provisions of this section, a Bench shall be presided over by the Chairman or a Vice-Chairman and shall consist of two other Members.
- (3) The Bench for which the Chairman is the Presiding Officer shall be the principal Bench and the other Benches shall be known as additional Benches.
- (4) Notwithstanding anything contained in sub-sections (1) and (2), the Chairman may authorise the Vice-Chairman or other Member appointed to one Bench to discharge also the functions of the Vice-Chairman or, as the case may be, other Member of another Bench.
- (5) Notwithstanding anything contained in the foregoing provisions of this section, and subject to any rules that may be made in this behalf, when one of the persons constituting a Bench (whether such person be the Presiding Officer or other Member of the Bench) is unable to discharge his functions owing to absence, illness or any other cause or in the event of the occurrence of any vacancy either in the office of the Presiding Officer or in the office of one or the other Members of the Bench, the remaining two persons may function as the Bench and if the Presiding Officer of the Bench is not one of the remaining two persons, the senior among the remaining persons shall act as the Presiding Officer of the Bench :

Provided that if at any stage of the hearing of any such case or matter, it appears to the Presiding Officer that the case or matter is of such a nature that it ought to be heard of by a Bench consisting of three Members, the case or matter may be referred by the Presiding Officer of such Bench to the Chairman for transfer to such Bench as the Chairman may deem fit.

[(5A) Notwithstanding anything contained in the foregoing provisions of this section, the Chairman may, for the disposal of any particular case, constitute a Special Bench consisting of more than three Members.]

- (6) Subject to the other provisions of this Chapter, the places at which the principal Bench and the additional Benches shall ordinarily sit shall be such as the Central Government may, by notification in the Official Gazette, specify [and the Special Bench shall sit at a place to be fixed by the Chairman.]

Vice-Chairman to act as Chairman or to discharge his functions in certain circumstances [Sec 245BB]

- (1) In the event of the occurrence of any vacancy in the office of the Chairman by reason of his death, resignation or otherwise, the Vice-Chairman or, as the case may be, such one of the Vice-Chairmen as the Central Government may, by notification in the Official Gazette, authorise in this behalf, shall act as the Chairman until the date on which a new Chairman, appointed in accordance with the provisions of this Chapter to fill such vacancy, enters upon his office.
- (2) When the Chairman is unable to discharge his functions owing to absence, illness or any other cause, the Vice-Chairman or, as the case may be, such one of the Vice-Chairmen as the Central Government may, by notification in the Official Gazette, authorise in this behalf, shall discharge the functions of the Chairman until the date on which the Chairman resumes his duties.

Power of Chairman to transfer cases from one Bench to another [Sec 245BC]

On the application of the assessee or the [Chief Commissioner or Commissioner] and after notice to them, and after hearing such of them as he may desire to be heard, or on his own motion without such notice, the Chairman may transfer any case pending before one Bench, for disposal, to another Bench.]

Decision to be taken by majority [Sec 245BD]

If the Members of a Bench differ in opinion on any point, the point shall be decided according to the opinion of the majority, if there is a majority, but if the Members are equally divided, they shall state the point or points on which they differ, and make a reference to the Chairman who shall either hear the point or points himself or refer the case for hearing on such point or points by one or more of the other Members of the Settlement Commission and such point or points shall be decided according to the opinion of the majority of the Members of the Settlement Commission who have heard the case, including those who first heard it.]

Application for settlement of cases [Sec 245C]

- (1) An assessee may, at any stage of a case relating to him, make an application in such form and in such manner as may be prescribed, and containing a full and true disclosure of his income which has not been disclosed before the [Assessing] Officer, the manner in which such income has been derived, the additional amount of income-tax payable on such income and such other particulars as may be prescribed, to the Settlement Commission to have the case settled and any such application shall be disposed of in the manner hereinafter provided :

Provided that no such application shall be made unless—

- (i) the additional amount of income-tax payable on the income disclosed in the application exceeds three lakh rupees; and
- (ii) such tax and the interest thereon, which would have been paid under the provisions of this Act had the income disclosed in the application been declared in the return of income before the Assessing Officer on the date of application, has been paid on or before the date of making the application and the proof of such payment is attached with the application.

- (1A) For the purposes of sub-section (1) of this section, the additional amount of income-tax payable in respect of the income disclosed in an application made under sub-section (1) of this section shall be the amount calculated in accordance with the provisions of sub-sections (1B) to (1D).

(1B) Where the income disclosed in the application relates to only one previous year,—

- (i) if the applicant has not furnished a return in respect of the total income of that year, then, tax shall be calculated on the income disclosed in the application as if such income were the total income;
- (ii) if the applicant has furnished a return in respect of the total income of that year, tax shall be calculated on the aggregate of the total income returned and the income disclosed in the application as if such aggregate were the total income.



- (1C) The additional amount of income-tax payable in respect of the income disclosed in the application relating to the previous year referred to in sub-section (1B) shall be,—
- in a case referred to in clause (i) of that sub-section, the amount of tax calculated under that clause;
 - in a case referred to in clause (ii) of that sub-section, the amount of tax calculated under that clause as reduced by the amount of tax calculated on the total income returned for that year;
- (1D) Where the income disclosed in the application relates to more than one previous year, the additional amount of income-tax payable in respect of the income disclosed for each of the years shall first be calculated in accordance with the provisions of sub-sections (1B) and (1C) and the aggregate of the amount so arrived at in respect of each of the years for which the application has been made under sub-section (1) shall be the additional amount of income-tax payable in respect of the income disclosed in the application.
- Every application made under sub-section (1) shall be accompanied by such fees as may be prescribed.
 - An application made under sub-section (1) shall not be allowed to be withdrawn by the applicant.
 - An assessee shall, on the date on which he makes an application under sub-section (1) to the Settlement Commission, also intimate the Assessing Officer in the prescribed manner of having made such application to the said Commission.*

Case Law:

- Application must disclose undisclosed income: The requirement is that there must be an income disclosed in a return furnished and undisclosed income disclosed to the Commission by a petition under section 245C – *CIT v. Damani Bros.* 259 ITR 475/126 Taxman 321

PROCEDURE FOR RECEIPT OF APPLICATION [Sec. 245D]

- On receipt of an application under section 245C, the Settlement Commission shall, within seven days from the date of receipt of the application, issue a notice to the applicant requiring him to explain as to why the application made by him be allowed to be proceeded with, and on hearing the applicant, the Settlement Commission shall, within a period of fourteen days from the date of the application, by an order in writing, reject the application or allow the application to be proceeded with:
 - A copy of every order under sub-section (1) shall be sent to the applicant and to the Commissioner.
- Where an application was made under section 245C before the 1st day of June, 2007, but an order under the provisions of sub-section (1) of this section, as they stood immediately before their amendment by the Finance Act, 2007, has not been made before the 1st day of June, 2007, such application shall be deemed to have been allowed to be proceeded with if the additional tax on the income disclosed in such application and the interest thereon is paid on or before the 31st day of July, 2007.
 Explanation.—In respect of the applications referred to in this sub-section, the 31st day of July, 2007 shall be deemed to be the date of the order of rejection or allowing the application to be proceeded with under sub-section (1).
- The Settlement Commission shall,—
 - in respect of an application which is allowed to be proceeded with under sub-section (1), within thirty days from the date on which the application was made; or
 - in respect of an application referred to in sub-section (2A) which is deemed to have been allowed to be proceeded with under that sub-section, on or before the 7th day of August, 2007, call for a report from the Commissioner, and the Commissioner shall furnish the report within a period of thirty days of the receipt of communication from the Settlement Commission.
- Where a report of the Commissioner called for under sub-section (2B) has been furnished within the period specified therein, the Settlement Commission may, on the basis of the report and within a period of fifteen days of the receipt of the report, by an order in writing, declare the application in question as invalid, and shall send the copy of such order to the applicant and the Commissioner:
- Where an application was made under sub-section (1) of section 245C before the 1st day of June, 2007 and an order under the provisions of sub-section (1) of this section, as they stood immediately before their amendment by the Finance Act, 2007, allowing the application to have been proceeded with, has been passed before the 1st day of June, 2007, but an order under the provisions of sub-section (4), as they stood immediately before their amendment by the Finance Act, 2007, was not passed before the 1st day of June, 2007,

such application shall not be allowed to be further proceeded with unless the additional tax on the income disclosed in such application and the interest thereon, is, notwithstanding any extension of time already granted by the Settlement Commission, paid on or before the 31st day of July, 2007.

(3) The Settlement Commission, in respect of—

- (i) an application which has not been declared invalid under sub-section (2C); or
- (ii) an application referred to in sub-section (2D) which has been allowed to be further proceeded with under that sub-section,

may call for the records from the Commissioner and after examination of such records, if the Settlement Commission is of the opinion that any further enquiry or investigation in the matter is necessary, it may direct the Commissioner to make or cause to be made such further enquiry or investigation and furnish a report on the matters covered by the application and any other matter relating to the case, and the Commissioner shall furnish the report within a period of ninety days of the receipt of communication from the Settlement Commission:

(4) After examination of the records and the report of the Commissioner, if any, received under—

- (i) sub-section (2B) or sub-section (3), or
- (ii) the provisions of sub-section (1) as they stood immediately before their amendment by the Finance Act, 2007,

and after giving an opportunity to the applicant and to the Commissioner to be heard, either in person or through a representative duly authorised in this behalf, and after examining such further evidence as may be placed before it or obtained by it, the Settlement Commission may, in accordance with the provisions of this Act, pass such order as it thinks fit on the matters covered by the application and any other matter relating to the case not covered by the application, but referred to in the report of the Commissioner.

(4A) The Settlement Commission shall pass an order under sub-section (4),—

- (i) in respect of an application referred to in sub-section (2A) or sub-section (2D), on or before the 31st day of March, 2008;
- (ii) in respect of an application made on or after the 1st day of June, 2007, within twelve months from the end of the month in which the application was made.

(5) Subject to the provisions of section 245BA, the materials brought on record before the Settlement Commission shall be considered by the Members of the concerned Bench before passing any order under sub-section (4) and, in relation to the passing of such order, the provisions of section 245BD shall apply.

(6) Every order passed under sub-section (4) shall provide for the terms of settlement including any demand by way of tax, penalty or interest, the manner in which any sum due under the settlement shall be paid and all other matters to make the settlement effective and shall also provide that the settlement shall be void if it is subsequently found by the Settlement Commission that it has been obtained by fraud or misrepresentation of facts.

(6A) Where any tax payable in pursuance of an order under sub-section (4) is not paid by the assessee within thirty-five days of the receipt of a copy of the order by him, then, whether or not the Settlement Commission has extended the time for payment of such tax or has allowed payment thereof by instalments, the assessee shall be liable to pay simple interest at one & one-fourth percent on the amount remaining unpaid from the date of expiry of the period of thirty-five days aforesaid.

(7) Where a settlement becomes void as provided under sub-section (6), the proceedings with respect to the matters covered by the settlement shall be deemed to have been revived from the stage at which the application was allowed to be proceeded with by the Settlement Commission and the income-tax authority concerned, may, notwithstanding anything contained in any other provision of this Act, complete such proceedings at any time before the expiry of two years from the end of the financial year in which the settlement became void.

(8) For the removal of doubts, it is hereby declared that nothing contained in section 153 shall apply to any order passed under sub-section (4) or to any order of assessment, reassessment or recomputation required to be made by the Assessing Officer in pursuance of any directions contained in such order passed by the



Settlement Commission and nothing contained in the proviso to sub-section (1) of section 186 shall apply to the cancellation of the registration of a firm required to be made in pursuance of any such directions as aforesaid.

Case laws:

- (1) Effect of omission of sub-section (1A) of section 245D: Where the applications of the respondents were not proceeded with only because of the objection raised by the Commissioner under sub-section (1A), having regard to the fact that the said sub-section (1A) was removed from the statute book subsequent to 1991, there was no reason why the Settlement Commission could not have entertained fresh applications under section 245C and this would not be a case of review at all - *CIT v. Bhaskar Picture Palace* 113 Taxman 109.
- (2) Power to over-rule objections is procedural: Amendment of section 245D with effect from 1-4-1979 empowering Settlement Commission to overrule objections of Commissioner was procedural and an order passed by Commissioner under section 245D prior to aforesaid amendment without giving applicant an opportunity of hearing was a nullity being passed in violation of principles of natural justice and after amendment of section 245D with effect from 1-4-1979 assessee was entitled to be heard on objections of Commissioner. *R.B. Shreeram Durga Prasad and Fatechand Nursing Das v. Settlement Commission (IT & WT)* 176 ITR 169/43 Taxman 34.

PROVISIONAL ATTACHMENT TO PROTECT REVENUE [Sec. 245DD]

If during the pendency of any proceedings the Commission is of the opinion that for the purpose of protecting the interests of the revenue, it is necessary to do so, it may attach provisionally for six months any property belonging to the applicant in the manner provided in the Second Schedule to the Act. Such attachment shall not extend in any case more than two years.

REOPENING OF COMPLETED PROCEEDINGS [Sec. 245E]

If the Commission is of the opinion that for the proper disposal of the case pending before it, it is necessary or expedient to reopen any proceedings connected with the case but which has been completed by any income-tax authority before the application was made, it may, with the concurrence of the applicant reopen such proceedings and pass such orders thereon as it thinks fit. However, no proceeding shall be reopened by the Commission under this provision if the period between the end of the assessment year to which such a proceeding relates and the date of application for settlement u/s. 245C exceed nine years.

Case Law:

- (1) Others/matters relating to jurisdiction of Settlement Commission: Failure on the part of the petitioner to deduct tax at source does not come within purview of section 245C(1). Section 245E contemplates reopening of completed proceedings not for benefit of assessee but in the interest of the revenue - *CIT v. Paharpur Cooling Towers (P.) Ltd.* 85 Taxman 357.

EXCLUSIVE JURISDICTION OF THE COMMISSION OVER THE ADMITTED APPLICATIONS [Sec. 245F]

After an application made u/s. 245C has been allowed to be proceeded with, the Commission will have exclusive jurisdiction over the case till an order u/s. 245D(4) has been made. During this period the Commission will have all the powers vested in an income-tax authority under the Act. However, in the absence of any express direction to the contrary by the Settlement Commission nothing contained in sec. 245F shall effect the operation of any other provisions of the Act requiring the applicant to pay tax on the basis of Self Assessment in relation to the matters before the Settlement Commission.

Case Law:

- (1) A final decision, however wrong, is still final and its binding force does not depend upon its correctness *Capital Cables (India) (P.) Ltd. v. Income-tax Settlement Commission* 267 ITR 528/139 Taxman 332

INSPECTION ETC REPORTS [Sec. 245G]

No persons shall be entitled to inspect or obtain copies of any reports made by any income-tax authority to the Settlement Commission but the Commission may in its discretion furnish copies thereof to any such person or an application made to in this behalf. However, for the purposes of enabling any person whose case is under consideration to rebut any evidence on record against him in any such report, the Commission shall furnish him a



certified copy of any such report if the applicant makes an application in this behalf. The copies will be supplied to the applicant on payment of the prescribed fee.

IMMUNITY FROM PROSECUTION AND PENALTY [Sec. 245H]

If the Commission is satisfied that any person who made the application for settlement has cooperated with the Commission in the proceedings before it and has made a full and true disclosure of his income and the manner in which such income has been derived, it may grant immunity from prosecution under the Income-tax Act or under the Indian Penal Code or under any other Central Act as also the imposition of any penalty under the Income-tax Act with respect to the case covered by the settlement. However, w.e.f. 1.6.2007 no such immunity shall be granted by the Commission in cases where the proceedings for prosecution for any such offence have been instituted before the date of receipt of the application under Section 245C. An immunity granted by the Commission shall stand withdrawn if the applicant fails to pay the sum specified in the order of settlement within the time specified in such order or within such further time as may be allowed by the Commission or fails to comply with any other condition subject to which the immunity was granted. The immunity may also be withdrawn if the Commission is satisfied that the applicant has, in the course of proceedings, concealed any particular material to the settlement or had given false evidence. Once the immunity granted is withdrawn, the assessee may be tried for offence with respect to which the immunity was granted or for any other offences of which he appears to have been guilty in connection with the Settlement and shall also become liable to imposition of any penalty under this Act to which such person would have been liable, had not such immunity been granted.

POWER OF SETTLEMENT COMMISSION TO SEND A CASE BACK TO THE ASSESSMENT OFFICER IF THE ASSESSEE DOES NOT COOPERATE [Sec. 245HA]

W.e.f. 1.6.2002 the power of Settlement Commission of sending the case back to the Assessing officer for non-cooperation of the applicant has been withdrawn and thereby requiring the Settlement Commission is required to decide the Settlement application admitted by it.

Credit for tax paid in case of abatement of proceedings [Sec. 245HAA]

Where an application made under section 245C on or after the 1st day of June, 2007, is rejected under sub-section (1) of section 245D, or any other application made under section 245C is not allowed to be proceeded with under sub-section (2A) of section 245D or is declared invalid under sub-section (2C) of section 245D or has not been allowed to be further proceeded with under sub-section (2D) of section 245D or an order under sub-section (4) of section 245D has not been passed within the time or period specified under sub-section (4A) of section 245D, the Assessing Officer shall allow the credit for the tax and interest paid on or before the date of making the application or during the pendency of the case before the Settlement Commission.

ORDER OF THE SETTLEMENT COMMISSION TO BE CONCLUSIVE [Sec. 245-I]

Order passed by the Commission u/s. 245D(4) is conclusive as to the matter stated therein and no matter covered by such order shall be reopened in any proceeding under this Act or under any other law for the time being in force save as provided under Chapter XIXA. The order of the Commission can only be challenged through a written petition under Article 226 of the Constitution of India in a High Court or through Special Leave Petition under Article 136 in the Supreme Court on the ground that while making such order, principles of the natural justice has been violated or mandatory procedural requirements of law were not complied with or if it is found that there is no nexus between the reasons given and the decision taken.

PAYMENT OF THE SUMS DUE UNDER ORDER OF SETTLEMENT [Sec. 245J]

Any sum specified in an order of settlement passed u/s. 245D(4) may be recovered and any penalty for default in making payment of such sum may be imposed and recovered in accordance with the provisions of Chapter XVII by the Assessing officer having jurisdiction over the person who made the application for settlement u/s. 245C.

BAR ON SUBSEQUENT APPLICATION FOR SETTLEMENT IN CERTAIN CASES [Sec. 254K]

In cases where an order has been passed u/s. 245D(4) providing for the imposition of penalty on the ground of concealment of particulars of income or after passing the order u/s. 245D(4), such person is convicted of any offence under Chapter XXII of the Income-tax Act in relation to that case or the case of such person is sent back to the Assessing officer u/s. 245BA, he shall not be entitled to apply for Settlement u/s. 245C in relation to any other matter.



PROCEEDINGS BEFORE THE COMMISSION TO BE JUDICIAL PROCEEDINGS [Sec. 245L]

Any proceedings under chapter XIXA before the Commission shall be deemed to be a judicial proceeding within the meaning of sec. 193 and 228, and for the purposes of sec. 196 of the Indian Penal Code.

ADVANCE RULING

Finance Act, 1993 inserted a chapter XIX-B in the Income-tax Act, 1961 to provide provisions of **Advance Rulings** to avoid dispute in respect of assessment of Income-tax liability in the case of non-resident. W.e.f. 1.10.1998, the scheme has been extended to cover notified resident applicants also. The chapter XIX-B contains sections 245N to 245V.

‘Advance Ruling’ means a determination by the Authority for Advance Rulings, in relation to (i) a transaction which has been undertaken or is proposed to be undertaken by a non-resident or by a resident with a non-resident, including a determination of a question of law or of fact, and (ii) issues relating to computation of income pending before the income-tax authority or the tribunal including a determination of a question of a law or of fact. [Sec. 245N(a)]

An application may be made by (i) non-resident, (ii) a resident entering into transaction with a non-resident, or (iii) a resident of the notified class or category i.e. a public sector company or a person indulging in a transaction with a non-resident. [Sec. 245N(b)]

Application for advance ruling should be in the prescribed form as below duly verified, along with a payment of fee of ₹ 2,500 shall be submitted to the authority for advance rulings.

Form No.	Classes of assessees
34C	Non- resident desires of obtaining an advance ruling.
34D	Resident persons seeking advance ruling in relation to a transaction with a non-resident.
34E	Resident person of notified class or category.

The application for advance rulings should be in quadruplicate and the applicant may withdraw such application within 90 days from the date of application. [Sec. 245Q]

An advance ruling shall not be allowed where (i) question of law or fact is already pending either before any income-tax authority or the Appellate Tribunal (except in case of a resident applicant of notified class or category) or any court, (ii) a transaction, which is designed for the avoidance of income-tax; or (iii) determination of the fair market value of any property. However, no application shall be rejected unless an opportunity has been given to the applicant of being heard and if the application is rejected, reasons for such rejection shall be given in the order. [Sec. 245R]

The Authority shall pronounce the advance ruling within six months after the receipt of the application. [Sec. 245R(6)]

In case an application for advance ruling has been made, in respect of an issue by a resident applicant, no Income-tax authority or the Appellate Tribunal shall give a decision on the same issue. [Sec. 245RR]

The advance ruling shall be binding only on the applicant who has sought it in respect of the specific transaction covered thereunder, on the Commissioner and the income-tax authorities subordinate to him, having jurisdiction over the applicant. The advance ruling will continue to remain in force unless there is a change either in law or in fact on the basis of which the advance ruling was pronounced. [Sec. 245S]

Case Laws:

- (i) Settlement Commission cannot be equated with CBDT for exercise of power of relaxation under section 119(2)(a) - *CIT v. Anjum M.H. Ghaswala* 119 Taxman 352/ 252 ITR 1.
- (ii) Commission is not bound to proceed with any application filed under section 245C - *CIT v. Hindustan Bulk Carriers* 259 ITR 449/126 Taxman 321.



STUDY NOTE - 26

TAX ADMINISTRATION

This Study Note includes

- Provisions under the Income Tax Act relating to Tax Administration

TAX ADMINISTRATION

INCOME TAX AUTHORITIES [Sec. 116]

In order to discharge executive and administrative functions relating to the Act, the following income-tax authorities have been constituted –

- (a) The Central Board of Direct Taxes;
- (b) Directors General of Income-tax or Chief Commissioners of Income-tax;
- (c) Directors of Income-tax or Commissioners of Income-tax or Commissioners of Income-tax (Appeals);
- (d) Additional Directors of Income-tax or Additional Commissioners of Income-tax or Additional Commissioners of Income-tax (Appeals);
- (e) Joint Directors of Income-tax or Joint Commissioners of Income-tax;
- (f) Deputy Director of Income-tax or Deputy Commissioner of Income-tax or Deputy Commissioner of Income-tax (Appeals);
- (g) Assistant Directors of Income-tax or Assistant Commissioners of Income-tax;
- (h) Income-tax Officers;
- (i) Tax Recovery Officers;
- (j) Inspectors of Income-tax.

APPOINTMENT OF INCOME-TAX AUTHORITIES [Sec. 117]

- (1) The Central Government may appoint such persons as it thinks fit to be income-tax authorities.
- (2) Without prejudice to the provisions of sub-section (1), and subject to the rules and orders of the Central Government regulating the conditions of service of persons in public services and posts, the Central Government may authorize the Board, or a Director-General, a Chief Commissioner or a Director or a Commissioner to appoint income-tax authorities below the rank of an Assistant Commissioner or Deputy Commissioner.
- (3) Subject to the rules and orders of the Central Government regulating the conditions of service of persons in public services and posts, an income-tax authority authorised in this behalf by the Board may appoint such executive or ministerial staff as may be necessary to assist it in the execution of its functions.

Control of income-tax authorities [Sec. 118]

The Board may, by notification in the Official Gazette, direct that any income-tax authority or authorities specified in the notification shall be subordinate to such other income-tax authority or authorities as may be specified in such notification.

CENTRAL BOARD OF DIRECT TAXES

The Central Board of Direct Taxes (CBDT) has been constituted under the Central Board of Revenue Act, 1963. It functions under the Ministry of Finance. The important powers of CBDT are:

- (i) To make rules for carrying out purposes of the Act [Sec. 295].
- (ii) To decide jurisdiction of the Income-tax Authorities [Sec. 120].



- (iii) To issue instructions, orders and directions to other Income-tax authorities for proper administration of this Act and all other persons employed in the execution of this Act. However, it cannot issue instructions to the Commissioner of Income-tax (Appeals). It cannot issue a direction to any Income-tax authority to dispose of a case in a particular manner. [Sec. 119],
- (iv) To declare an organization as company [Sec. 2(17) (iv)].
- (v) To entertain objections in respect of search and seizure under the Act. [Sec.132].
- (vi) To relax the provisions of Sections 139, 143, 144, 147, 148, 154, 155, 158BFA, 201(1A), 210, 211, 234A, 234B, 234C, 271 and 273 or otherwise [Section 119(2)(a)].
- (vii) Power of relaxing any requirement contained in Chapter IV (provisions for computation of income under various heads) or Chapter VI-A (provisions for deductions from gross total income) [Section 119(2)(c)].
- (viii) Issue such general or special orders for relaxation of the provisions of sections relating to FBT viz; 115WD, 115WE, 115WF, 115WG, 115WH, 115WJ and 115WK [Section 119(2)(a)].
- (ix) Prescribe categories of transactions and documents pertaining to business or profession, where quoting of PAN is necessary [Sec, 139A].
- (x) Frame a scheme in respect of 'Tax Return Preparers' [Sec. 139B].
- (xi) Prescribe class of persons by whom return of income [Sec. 139D] and TDS statements [Sec. 200] should be filed electronically.
- (xii) Prescribing qualifications for Authorized Representatives [Sec. 288].
- (xiii) Condone delay for seeking CBDT's approval, where it is required [Sec. 293B] and authorize any income tax authority not being Commissioner of Income-tax (Appeals), to admit belatedly ant claim for exemption, deduction, refund or relief [Section 119(2)(b)].
- (xiv) To prescribe method for computation of arm's length price [Section 92C].and to prescribe record to be kept and the time for which it is to be preserved [Section 92D].

Circulars issued by the CBDT are legally binding on the revenue and this binding character attaches to the circulars even if they are found not in accordance with the correct interpretation of a statutory provision and they depart or deviate from such construction - *K.P. Varghese v. ITO 131 ITR 597 (SC)*.

It is well-settled that circulars can bind the ITO but will not bind the appellate authority or the Tribunal or the Court or even the assessee - *CIT v. Hero Cycles (P.) Ltd. 228 ITR 463 (SC)*.

CBDT has power, interalia, to tone down the rigor of the laws and ensure fair enforcement of its provision by issuing circular.

Circular contemplated in sec.119 (2)(a) cannot be adverse to the assessee. Power is given for the purpose of just, proper and efficient management of work of assessment. Circular, however are not meant for contradicting or nullifying any provision of the statue. They are meant to mitigate the rigor of application of a particular provision. So long as such a circular is in favour, it would be binding on the departmental authorities in view of the provision of sec. 119 to ensure a uniform and proper administration & application of the IT Act - *UCO Bank V CIT 237 ITR 899 (SC)*.

DIRECTOR GENERAL/DIRECTOR

The Central Government has power to appoint Director General and Director [Sec. 117]. The CBDT authorize them to perform such functions as may be assigned to them by [Sec. 120]. The powers enjoyed by them include:

- (i) To appoint an Income-tax authority below the rank of Assistant Commissioner/Deputy Commissioner, if authorised by the Board [Sec. 117].
- (ii) To direct the Joint Commissioner to function and assume the powers of assessing officer, if so authorised by the Board [Sec. 120].

- (iii) To transfer cases from one or more assessing officers to any other assessing officer who is subordinate to him [Sec. 127].
- (iv) To enquire or investigate concealed income of any person within his jurisdiction [Sec. 131(1A)].
- (v) Authorise any Joint Director / Joint Commissioner, Deputy Director / Deputy Commissioner, Assistant Director / Assistant Commissioner or Assessing Officer to enter, search and seize valuables [Sec. 132(1)].
- (vi) To requisition books of accounts, etc.[Sec. 132A].
- (vii) To survey [Sec. 133A].
- (viii) To make an enquiry [Sec. 135].
- (ix) To collect certain information [Sec. 133B]

COMMISSIONERS OF INCOME TAX / CHIEF COMMISSIONERS OF INCOME TAX

The Central Government has power to appoint Director General and Director [Sec. 117]. The CBDT authorize them to perform such functions as may be assigned to them by [Sec. 120]. The powers enjoyed by them include:

- (i) To appoint an Income-tax authority below the rank of Assistant Commissioner/Deputy Commissioner, if authorised by the Board – [Sec. 117].
- (ii) To direct the Joint Commissioner to function and assume the powers of assessing officer, if so authorised by the Board – [Sec. 120].
- (iii) To transfer cases from one or more assessing officers to any other assessing officer who is subordinate to him – [Sec. 127].
- (iv) To enquire or investigate conceal income of any person within his jurisdiction – [Sec. 131(1A)].
- (v) To authorise any Joint Director/Joint Commissioner, Deputy Director/Deputy Commissioner, Assistant Director/Assistant Commissioner or Assessing Officer to enter, search and seize valuables – [Sec. 132(1)].
- (vi) To requisition books of accounts, etc. – [Sec. 132A].
- (vii) To survey – [Sec. 133A].
- (viii) To make an enquiry – [Sec. 135].
- (ix) To collect certain information– [Sec. 133B]

Additional Powers

- (i) Power regarding discovery, production of evidence, etc. [Sec. 131].
- (ii) To sanction reopening of assessments after the expiry of four years. [Sec.151(1)].
- (iii) To direct the Assessing Officer to prefer appeal to the Tribunal against the order of First Appellate Authority. [Sec. 253(2)]
- (iv) Request the Tribunal to file Reference to High Court. [Sec. 256].
- (v) To revise any order passed by the Assessing Officer that is prejudicial to revenue. [Sec. 263].
- (vi) To revise any order passed by a subordinate authority on an application by the assessee or *suo moto* when the revision is in favour of the assessee. [Sec.264]

COMMISSIONER OF INCOME-TAX (APPEALS)

Appointment is made by the Central Government. The following are important powers:

- (i) Power regarding discovery, production of evidence etc. [Sec. 131]



- (ii) To condone delay in filing of appeal.
- (iii) Power to call for information. [Sec. 133]
- (iv) Power to inspect register of companies. [Sec. 134]
- (v) To dispose of an appeal and to confirm, reduce, enhance or annul the assessment [Sec. 251]
- (vi) Power to impose a penalty. [Sec. 271]
- (vii) Power to set off any refund against arrears of tax. [Sec. 245].
- (viii) The Commissioner (Appeals) has inherent powers to stay recovery proceedings *Paulsons Litho Works v. ITO* 208 ITR 676 (Mad.).

JOINT COMMISSIONER OF INCOME TAX

They are appointed by the Central Government. They enjoy the following powers :-

- (i) Power regarding discovery, production of evidence, etc. [Sec. 131]
- (ii) Power of search and seizure, if authorised. [Sec. 132]
- (iii) Power to call for information. [Sec. 133]
- (iv) Power to survey- [Sec. 133A]
- (v) Power to make an enquiry- [Sec. 135]
- (vi) Power to collect certain information- [Sec. 133B]
- (vii) Power to inspect register of companies. [Sec. 134]
- (viii) To sanction reopening of assessment after the expiry of 4 years, if the assessment is made under any section other than sections 143(3) and 147.

ASSESSING OFFICER

‘Assessing Officer’ means the Assistant Commissioner or Deputy Commissioner or Assistant Director or Deputy Director or the Income-tax Officer who is vested with the relevant jurisdiction by virtue of directions or orders issued under Section 120 or any other provision of this Act, and the *Additional Commissioner or Additional Director or Joint Commissioner or Joint Director* who is directed under the said section 120 to exercise or perform all or any of the powers and functions conferred on, or assigned to, an Assessing Officer under this Act [Sec. 2(7A)]

The following are some of the powers of Income-tax Officers —

- (i) Power regarding discovery, production of evidence, etc. [Sec. 131]
- (ii) Power of search and seizure, if authorised. [Sec. 132]
- (iii) Power to requisition books of accounts. [Sec. 132A]
- (iv) To apply the assets seized and retained u/s. 132 in satisfaction of the existing liabilities of the assessee under Direct Taxes Act. [Sec. 132B]
- (v) Power to call for information. [Sec. 133]
- (vi) Power to collect certain information- [Sec. 133B]
- (vii) Power to inspect register of companies. [Sec. 134]
- (viii) Power to allot permanent account number. [Sec. 139A]
- (ix) Power to direct an assessee to get his accounts audited. [Sec. 142]
- (x) Power to make assessment. [Sec. 143, 144]
- (xi) Power to reassess income which has escaped assessment.[sec. 147]
- (xii) Power to rectify mistakes apparent from the records, either on his own or on an application made by the assessee. [Sec. 154]

- (xiii) Power to grant a certificate to an assessee to receive a payment without deduction of tax at source or deduction of tax at source at a lower rate than prescribed [Secs. 194, 195, 197]
- (xiv) Power to impose penalty for default in payment of a tax. [Sec. 221]
- (xv) Power to grant refund. [Sec. 237, 240]
- (xvi) Power to withhold refund in certain cases [Sec. 241]
- (xvii) Power to adjust the refund against any demand of tax etc. outstanding against the assessee. [Sec. 245].
- (xviii) Power to impose penalty for the prescribed defaults under the Act [Chapter XXI]
- (xix) Power to initiate prosecution for the prescribed offences under the Act [Chapter XXII]
- (xx) Power to determine arm's length price of international transactions [Sec. 92C]

INSPECTORS OF INCOME TAX

Inspectors are appointed by the Commissioner of Income Tax.

They have to perform such functions as are assigned to them by the Commissioner or any other Income-tax authority under which they are appointed to perform their functions.

In case of survey, inspectors have power to inspect books of account and other documents, place marks of identification, to take statements at any function, ceremony or event [Sec. 133A].

Change of incumbent of an office [Sec. 129]

Whenever in respect of any proceeding under this Act an income-tax authority ceases to exercise jurisdiction and is succeeded by another who has and exercises jurisdiction, the income-tax authority so succeeding may continue the proceeding from the stage at which the proceeding was left by his predecessor :

Provided that the assessee concerned may demand that before the proceeding is so continued the previous proceeding or any part thereof be reopened or that before any order of assessment is passed against him, he be reheard.



STUDY NOTE - 27

TAXATION OF INTERNATIONAL TRANSACTIONS

This Study Note includes

- Provisions under the Income Tax Act relating to Transfer Pricing

1. INTRODUCTION

The Finance Act 2001 has introduced detailed provisions relating to transfer pricing, requiring all 'international transactions' between 'associated enterprises' to be at arm's length. These provisions are applicable with effect from 1 April 2001.

The provisions are exhaustive in many respects and generally in line with international practices prescribing methodologies, documentation requirements and penalties.

Scope of application of the Provisions

Any income / expense arising from an international transaction with an associated enterprise must be computed having regard to the arm's-length price. Also, costs or expenses allocated or apportioned between two or more associated enterprises should be determined having regard to arm's-length prices.

The transfer pricing provisions are wide enough to cover transactions between a foreign entity and its permanent establishment in India.

The transfer pricing provisions would not apply in cases wherein the application of arm's length price results in a downward revision in the income chargeable to tax in India.

2. INTERNATIONAL TRANSACTIONS

- The term covers a wide range of revenue and capital transactions between two or more associated enterprises where either or both are non-residents;
- The term also includes arrangements between associated enterprises for cost-sharing in connection with benefits, services or facilities provided to any of such enterprises.

Additionally, another type of transaction is deemed to be an international transaction between two associated enterprises. This is when an enterprise, say X, has entered into a transaction with an unassociated person, say A Ltd. and there exists a prior agreement in relation to this transaction between A Ltd and Y Ltd. (an associated enterprise of X); or the terms of this transaction are determined in substance between A Ltd and Y Ltd.

3. ASSOCIATED ENTERPRISE

The term 'associated enterprise' has been defined in a broad manner. Based on the same, the following illustrates the definition when Enterprise X ("X") would be the associated enterprise of Enterprise Y ("Y") :

- X participates, directly or indirectly, or through one or more intermediaries, in the management, control or capital of Y and one or more of the requisites enlisted below are fulfilled; or
- The same persons participate in the management, control or capital of X, as also that of Y and one or more of the requisites enlisted below are fulfilled.

X and Y would be deemed to be associated enterprises if at any time during the previous year :

- X holds directly or indirectly shares carrying at least 26% voting power in Y or vice versa;
- Any person holds directly or indirectly shares carrying at least 26% voting power in both X and Y;
- A loan advanced by X to Y amounts to at least 51% of book value of the total assets of Y or vice versa;
- X guarantees at least 10% of the total borrowings of Y or vice versa;
- More than half of the directors or members of the governing board, or one or more of the executive directors or executive members of the governing board of X are appointed by Y or vice versa;
- More than half of the directors or members of the governing board, or one or more of the executive directors or members of the governing board of X and Y are appointed by the same person(s);
- The manufacture / processing of goods/articles by, or business of, X, is wholly dependent on use of intangibles or any other commercial rights of similar nature, or any data, documentation or drawing etc., owned by Y or for which Y has exclusive rights; or
- At least 90% of raw materials for the manufacture or processing of goods or articles required by X are supplied by Y or persons specified by Y under commercial terms influenced by Y or;
- Goods / articles manufactured / processed by X are sold to Y or persons specified by Y, and Y influences the commercial terms relating to the sale or;
- X is controlled by Mr. A and Y is controlled by Mr. A or relative of Mr. A either individually or jointly;
- X is controlled by a Hindu Undivided Family, and Y is controlled by a member of such Hindu Undivided Family or by a relative of a member of such Hindu Undivided Family, or jointly by such member and his relative; or
- X is a firm, association of persons or body of individuals, and Y holds at least 10% interest in such firm, association of persons or body of individuals; or
- There exists, between X and Y, any relationship of mutual interest, as may be prescribed (no such relationship has yet been prescribed).

What is arm's length price?

Answer : It means a price which is applied or proposed to be applied in a transaction -

- (a) Between persons other than associated enterprises,
- (b) In uncontrolled conditions.

Methods of Computation [Section 92C]; The arm's length price in relation to an international transaction shall be determined by any of the following methods -

- (a) Comparable Uncontrolled Price Method,
- (b) Resale Price Method,
- (c) Cost plus Method,
- (d) Profit Split Method,
- (e) Transactional Net Margin Method,
- (f) Such other method as may be prescribed by the Board.

COMPUTATION OF ALP USING COMPARABLE UNCONTROLLED PRICE METHOD

Step I: Identify the price charged / paid for property transferred or services provided in a **comparable uncontrolled transaction(s)**.

Step II: **Adjust** the price derived in Step I above **for differences**, if any, which could materially affect the price in the open market.

- (a) between the international transaction and the comparable uncontrolled transactions, or
- (b) between the enterprises entering into such transactions.

Step III: Arm's Length Price = Step I **Add/Less:** Step II



Illustration 1. Jackle, Korea and CD Ltd, an Indian Company are associated enterprises. CD Ltd manufactures Cel Phones and sells them to Jackle, Korea & Fox, a Company based at Nepal. During the year CD Ltd supplied 2,50,000 Cellular Phones to Jackle Korea at a price of ₹ 3,000 per unit and 35,000 units to Fox at a price of ₹ 5,800 per unit. The transactions of CD Ltd with Jackle and Fox are comparable subject to the following considerations -

- (a) Sales to Jackle are on FOB basis, sales to Fox are CIF basis. The freight and insurance paid by Jackle for each unit is ₹ 700.
- (b) Sales to Fox are under a free warranty for Two Years whereas sales to Jackle are without any such warranty. The estimated cost of executing such warranty is ₹ 500.
- (c) Since Jackle's order was huge in volume, quantity discount of ₹ 200 per unit was offered to it.

Compute the Arm's Length Price and the amount of increase in the Total Income of CD Ltd, if any, due to such Arm's Length Price.

A. Computation of Arm's Length Price of Products sold to Jackle Korea by CD Ltd.

Particulars	₹	₹
Price per Unit in a Comparable Uncontrolled Transaction		5,800
Less: Adjustment for Differences -		
(a) Freight and Insurance Charges	700	
(b) Estimated Warranty Costs	500	
(c) Discount for Voluminous Purchase	200	(1,400)
Arms's Length Price for Cellular Phone sold to Jackle Korea		4,400

B. Computation of Increase in Total Income of CD Ltd

Particulars	₹
Arm's Length Price per Unit	4,400
Less: Price at which actually sold to Jackle Korea	(3,000)
Increase in Price per Unit	1,400
No. of Units sold to Jackle Korea	2,50,000
Therefore, increase in Total Income of CD Ltd (2,50,000 × ₹ 1,400)	₹ 35 Crores.

RESALE PRICE METHOD

Step I : Identify the price at which property purchased or services obtained by the enterprise from an associated enterprise is resold or are provided to an **unrelated enterprise**.

Step II: Reduce the normal GP margin accruing to the enterprise or to an unrelated enterprise from the purchase and resale of the same or similar property or from II) obtaining and providing the same or similar services, in a comparable uncontrolled transaction (s).

Step III: Reduce expenses incurred by the enterprise in connection with the purchase of property or obtaining of services.

Step IV: Adjust for functional and other differences, including differences in accounting practices, if any, between the international transaction and the comparable uncontrolled transactions, or between the enterprises entering into such transactions, which could materially affect the amount of gross profit margin in the open market.

Step V: Arm's Length Price = Step I

Less Step II & III

Add / Less Step IV.

Illustration 2. Swinhoe LLP of France and Rani Ltd of India are associated enterprises. Rani Ltd. imports 3,000 compressors for Air Conditioners from Swinhoe at ₹ 7,500 per unit and these are sold to Paharpur Cooling Solutions Ltd at a price of ₹ 11,000 per unit. Rani had also imported similar products from Cold Ltd and sold outside at a Gross Profit of 20% on Sales.

Swinhoe offered a quantity discount of ₹ 1,500 per unit. Cold could offer only ₹ 500 per unit as Quantity Discount. The freight and customs duty paid for imports from Poland had cost Rani ₹ 1,200 a piece. In respect of purchase from Cold Ltd, Rani had to pay ₹ 200 only as freight charges.

Determine the Arm's Length Price and the amount of increase in Total Income of Rani Ltd.

A. Computation of Arm's Length Price of Products bought from Swinhoe, France by Rani Ltd.

Resale Price of Goods Purchased from Swinhoe	11,000
Less: Adjustment for Differences –	
(a) Normal Gross Profit Margin at 20% of Sale Price [20% × ₹ 11,000]	2,200
(b) Incremental Quantity Discount by Swinhoe [₹ 1,500 – ₹ 500]	1,000
(c) Difference in Purchase related Expenses [₹ 1,200 – ₹ 200]	1,000
Arms Length Price	6,800

B. Computation of Increase in Total Income of Rani Ltd

Particulars	₹
Price at which actually bought from Swinhoe LLP of France	7,500
Less : Arms Length Price per unit under Resale Price Method	(6,800)
Decrease in Purchase Price per Unit	700
No. of Units purchased from Swinhoe	1,000
Therefore, increase in Total Income of Rani Ltd [3,000 Units × ₹ 700]	₹ 21,00,000

COST PLUS METHOD IN DETERMINING ALP

Step I: Determine the direct and indirect costs of production incurred by the enterprise in respect of property transferred or services provided to an associated enterprise.

Step II: Determine the normal GP mark-up to such costs (computed under same accounting norms) arising from the transfer or provision of the same or similar property or services by the enterprise, or by an unrelated enterprise, in a comparable uncontrolled transaction(s).

Step III: Adjust the normal gross profit mark-up referred to in Step II to take into account the functional and other differences, if any, between the international transaction and the comparable uncontrolled transactions, or between the enterprises entering into such transactions, which could materially affect such profit mark-up in the open market.

Step IV: Arm's Length Price = Step I
Add Step III

Illustration 3. Branco Inc., a French Company, holds 45% of Equity in the Indian Company Chirag Technologies Ltd (CTL). CTL is engaged in development of software and maintenance of the same for customers across the globe. Its clientele includes Branco Inc.

During the year, CTL had spent 2,400 Man Hours for developing and maintaining software for Branco Inc, with each hour being billed at ₹ 1,300. Costs incurred by CTL for executing work for Branco Inc. amount to ₹ 20,00,000.

CTL had also undertaken developing software for Harsha Industries Ltd for which CTL had billed at ₹ 2,700 per Man Hour. The persons working for Harsha Industries Ltd and Branco were part of the same team and were of matching credentials and caliber. CTL had made a Gross Profit of 60% on the Harsha Industries work.



CTL's transactions with Branco Inc. are comparable to the transactions with Harsha Industries, subject to the following differences:

- (a) Branco gives technical know how support to CTL which can be valued at 8% of the Normal Gross Profit. Harsha Industries does not provide any such support.
- (b) Since the work for Branco involved huge number of man hours, a quantity discount of 14% of Normal Gross Profits was given.
- (c) CTL had offered 90 Days credit to Branco the cost of which is measured at 2% of the Normal Billing Rate, No such discount was offered to Harsha Industries Ltd.

Compute ALP and the amount of increase in Total Income of Chirag Technologies Ltd.

(A) Computation of Arms Length Gross Profit Mark-up

Particulars	%	%
Normal GP Mark Up		60
Less: Adjustment for Differences		
(a) Technical Support from Branco 8% of Normal GP	4.8	
[8% of 60%]		
(b) Quantity Discount 14% of Normal GP [14% of 60%]	8.4	(13.2)
		46.8
Add: Cost of Credit to Branco 2% of Normal Bill [2% × GP 60%]	1.2	1.2
Arms Length Gross Profit Mark-up		48

(B) Computation of Increase in Total Income of Branco Ltd

Particulars	₹
Cost of Services Provided to CTL	20,00,000
Arms Length Billed Value	
[Cost / (100 - Arms' Length Mark up)]	
[= ₹ 20,00,000 / (100% - 48%)]	38,46,154
Less:	(31,20,000)
Therefore, increase in Total Income of Branco	7,26,154

PROFIT SPLIT METHOD

This method is mainly applicable in international transactions involving transfer of unique intangibles or in multiple international transactions which are so inter-related that they cannot be evaluated separately for the purpose of determining the Arm's Length Price of any one transaction.

Step I: Determine the combined net profit of the associated enterprises arising from the international transaction in which they are engaged.

Step II: Determine the relative contribution made by each of the associated enterprises to the earning of such combined net profit. This is determined on the basis of the functions performed, assets employed and risks assumed by each enterprise and on the basis of reliable external market data which indicates how such contribution would be determined by unrelated enterprises performing comparable functions in similar circumstances.

Step III: Split the combined net profit amongst the enterprises on the basis of reasonable returns and in proportion to their relative contributions, as determined in Step II. (See note below)

Step IV: Arm's Length Price - Profit apportioned to the assessee under Step III.

Note : Combined Net Profit shall be split as under:

III.A. First Split = Reasonable Return: Allocate an amount to each enterprise so as to provide it with a basic return appropriate for the type of international transaction with reference to market returns achieved in similar types of transactions by independent enterprises.

III.B. Second Split = Contribution Ratio: Allocate the residual net profit amongst the enterprises in proportion to their relative contribution.

III.C. Total Profit: Share of profit of each enterprise = Step III.A + III.B

Illustration 4. NBR Medical Equipments Inc. (NBR) of Canada has received an order from a leading UK based Hospital for development of a hi-tech medical equipment which will integrate the best of software and latest medical examination tool to meet varied requirements. The order was for 3,00,000 Euros. To execute the order, NBR joined hands with its subsidiary Precision Components Inc. (PCI) of USA and Bioinformatics India Ltd (BIL), an Indian Company. PCI holds 30% of BIL. NBR paid to PCI and BIL Euro 90,000 and Euro 1,00,000 respectively and kept the balance for itself. In the entire transaction, a profit of Euro 1,00,000 is earned. Bioinformatics India Ltd incurred a Total Cost of Euro 80,000 in execution of its work in the above contract. The relative contribution of NBR, PCI and BIL may be taken at 30%, 30% and 40% respectively. Compute the Arm's Length Price and the incremental Total Income of Bioinformatics India Ltd, if any due to adopting Arms Length Price determined here under.

Particulars	Euros
A. Share of each of the Associates in the Value of the Order	3,00,000
Value of the Order	
Share of BIL [Given]	1,00,000
Share of PCI [Given]	90,000
Share of NBR [Amount Retained = 3,00,000 – 1,00,000 - 90,000]	1,10,000
B. Share of each of the Associates in the Profit of the Order	1,00,000
Combined Total Profits	
Share of BIL [Contribution of 40% × Total Profit • 1,00,000]	40,000
Share of PCI [Contribution of 30% × Total Profit • 1,00,000]	30,000
Share of NBR [Contribution of 30% × Total Profit • 1,00,000]	30,000
C. Computation of Incremental Total Income of BIL	
Total Cost to Bioinformatics India Ltd	80,000
Add: Share in the Profit to BIL (from B above)	40,000
Revenue of BIL on the basis of Arm's Length Price	1,20,000
Less: Revenue Actually received by BIL	(1,00,000)
Increase in Total Income of BIL	20,000

TRANSACTION NET MARGIN METHOD

Step I: Compute the net profit margin realised by the enterprise from an international transaction entered into with an associated enterprise, in relation to costs incurred or sales effected or assets employed by enterprise or having regard to any other relevant base.

Step II: Compute the net profit margin realised by the enterprise or by an unrelated enterprise from a **comparable uncontrolled transaction (s)**, having regard to the same base as in Step I.

Step III: Adjust the net profit margin as per Step II for differences, if any, which could materially affect amount of net profit margin in the open market :

- between the international transaction and the comparable uncontrolled transactions, or
- between the enterprises entering into such transactions.



Step IV: Net Profit Margin for uncontrolled transactions = Step II **Add/Less** Step III.

Step V: Arm's Length Price = Transaction Value x Net Profit Margin as per Step IV above.

Meaning of certain terms: For the computation of Arm's Length Price -

1. **"Transaction"** includes a number of closely linked transactions.
2. **"Uncontrolled Transaction"** means a transaction between unrelated enterprises, whether resident or non-resident.
3. **"Unrelated Enterprises"**: Enterprises are said to be unrelated, if they are not associated or deemed to be associated u/s 92A.
4. **"Uncontrolled conditions"**: Conditions which are not controlled or suppressed or moulded for achievement of pre-determined results are said to be uncontrolled conditions.
5. **"Property"** includes goods, articles or things, and intangible property.
6. **"Services"** include financial services.

Illustration 5. Fox Solutions Inc. a US Company, sells Laser Printer Cartridge Drums to its Indian Subsidiary Quality Printing Ltd at \$ 20 per drum. Doc Solutions Inc. has other takers in India for its Cartridge Drums, for whom the price is \$ 30 per drum. During the year, Fox Solutions had supplied 12,000 Cartridge Drums to Quality Printing Ltd.

Determine the Arm's Length Price and taxable income of Quality Printing Ltd if its income after considering the above is ₹ 45,00,000. Compliance with TDS provisions may be assumed and Rate per USD is ₹ 45. Also determine income of Doc Solutions Inc.

A. Computation of Total Income of Quality Printing Ltd.

Particulars	₹	₹
Total Income before adjusting for differences due to Arm's Length Price		
Add: Difference on Account of Adopting Arm's Length Price	1,08,00,000	
Amount actually paid to Doc Solutions [12,000 × \$ 20 × ₹ 45]	(1,62,00,000)	
Less: Amount under Arms Length Price [12,000 × \$ 30 × ₹ 45]	<u>54,00,000</u>	
Incremental Cost on adopting ALP		
U/s 92(3), Taxable Income cannot be reduced on applying ALP.		
Therefore, difference on account of ALP is ignored.		
Total Income of Quality Printing Ltd		45,00,000

B. Computation of Total Income of Fox Solutions Inc.

The provisions relating to taxing income of Fox Solutions Inc., on applying Arm's Length Price for transactions entered into by a Foreign Company is given in Circular 23 dated 23.7.1969, which is as follows:

- (i) **Transactions Not Taxable in India** : Transactions will not be subject tax in India if transactions are on principal-to-principal basis and are entered into at ALP, and the subsidiary also carries on business on its own.
- (ii) **Transactions Taxable in India** if the Indian Subsidiary does not carry on any business on its own. The following are the other considerations in this regard -
 - (i) Adopting ALP does not affect the computation of taxable income of Fox Solutions Inc. if tax has been deducted at source or if tax is deductible.
 - (ii) Where ALP is adopted for taxing income of the Parent Company, income of the recipient Company (i.e. Quality Printing Ltd) will not be recomputed.

Illustration 6. Khazana Ltd is an Indian Company engaged in the business of developing and manufacturing Industrial components. Its Canadian Subsidiary Techpro Inc. supplies technical information and offers technical support to Khazana for manufacturing goods, for a consideration of Euro 1,00,000 per year.

Income of Khazana Ltd is ₹ 90 Lakhs. Determine the Taxable Income of Khazana Ltd if Techpro charges Euro 1,30,000 per year to other entities in India. What will be the answer if Techpro charges Euro 60,000 per year to other entities. (Rate per Euro may be taken at ₹ 50.)

Computation of Total Income of Khazana Ltd.

Particulars	₹ (Lakhs)	₹ (Lakhs)
When Price Charged for Comparable Uncontrolled Transaction is	€ 1,00,000	€ 50,000
Price actually paid by Khazana Ltd [1,00,000 × ₹ 50]	50	50
Less: Price Charged in Rupees (under ALP) [1,30,000×50]/[60,000×50]	65	30
Incremental Profit on adopting ALP [A]	(15)	20
Total Income before adjusting for differences due to Arm's Length Price		
Add: Difference on Account of Adopting Arm's Length Price (if [A] is positive)	90	9020
Total Income of Khazana Ltd	90	110

Note : U/s 92(3), Taxable Income cannot be reduced on applying ALP. Therefore, difference on account of ALP which reduces the Taxable Income is ignored.



STUDY NOTE - 28

DOUBLE TAXATION RELIEF

This Study Note includes

- Provisions under the Income Tax Act relating to Double Taxation Relief

DOUBLE TAXATION RELIEF

28.1 AGREEMENT WITH FOREIGN COUNTRIES [Sec 90]

- (1) The Central Government may enter into an agreement with the Government of any country outside India—
 - (a) for the granting of relief in respect of—
 - (i) Income on which have been paid both income-tax under this Act and income-tax in that country; or
 - (ii) income-tax chargeable under this Act and under the corresponding law in force in that country to promote mutual economic relations, trade and investment, or
 - (b) For the avoidance of double taxation of income under this Act and under the corresponding law in force in that country, or
 - (c) For exchange of information for the prevention of evasion or avoidance of income-tax chargeable under this Act or under the corresponding law in force in that country, or investigation of cases of such evasion or avoidance, or
 - (d) for recovery of income-tax under this Act and under the corresponding law in force in that country, and may, by notification in the Official Gazette, make such provisions as may be necessary for implementing the agreement.
- (2) Where the Central Government has entered into an agreement with the Government of any country outside India under sub-section (1) for granting relief of tax, or as the case may be, avoidance of double taxation, then, in relation to the assessee to whom such agreement applies, the provisions of this Act shall apply to the extent they are more beneficial to that assessee.
- (3) Any term used but not defined in this Act or in the agreement referred to in sub-section (1) shall, unless the context otherwise requires, and is not inconsistent with the provisions of this Act or the agreement, have the same meaning as assigned to it in the notification issued by the Central Government in the Official Gazette in this behalf.

Explanation.

For the removal of doubts, it is hereby declared that the charge of tax in respect of a foreign company at a rate higher than the rate at which a domestic company is chargeable, shall not be regarded as less favorable charge or levy of tax in respect of such foreign company.

28.2 COUNTRIES WITH WHICH NO AGREEMENT EXISTS [Sec. 91]

- (1) If any person who is resident in India in any previous year proves that, in respect of his income which accrued or arose during that previous year outside India (and which is not deemed to accrue or arise in India), he has paid in any country with which there is no agreement under section 90 for the relief or avoidance of double taxation, income-tax, by deduction or otherwise, under the law in force in that country, he shall be entitled to the deduction from the Indian income-tax payable by him of a sum calculated on such doubly taxed income at the Indian rate of tax or the rate of tax of the said country, whichever is the lower, or at the Indian rate of tax if both the rates are equal.

In the other words, where section 90 does not apply, unilateral relief will be available, if the following conditions are satisfied:

- (i) The assessee in question must have been resident in India in the previous year.
- (ii) That some income must have accrued or arisen to him outside India during the previous year & it should also be received outside India. Such income must not be deemed to accrue or arise in India.
- (iii) The income should be taxed in India & in a foreign country & there should be no reciprocal arrangements for relief or avoidance on double taxation with the country where income has accrued or arisen.
- (iv) In respect of that income, the assessee must have paid by deduction or other wise, tax under the law in force in the foreign country in question in which the income outside India has arisen.

In all the above conditions are satisfied, such person shall be entitled to deduction from the Indian Income-tax payable by him of a sum calculated on such doubly taxed income-

- (a) at the average Indian rate of tax or the average of tax of the said country, whichever is lower, or
- (b) at the Indian rate of tax if both the rates are equal.

Average rate of tax means the tax payable on total income, after deduction of any relief due under the provision of this act but before deduction of any relief due under this chapter, divided by the total income.

ILLUSTRATIONS ON DOUBLE TAXATION RELIEF

Illustration 1. R a resident Indian, has derived the following income for the previous year relevant to the assessment year 2012-2013.

Particulars	₹
(1) Income from profession	3,00,000
(2) Share income from a partnership in country X (tax paid in country Y for this income in equivalent Indian rupees ₹ 25,000)	2,00,000
(3) Commission income from a concern in country Y (tax paid in country Y at 20%) converted in Indian rupee.	40,000
(4) Interest from schedule banks.	20,000

R wishes to know whether he is eligible to any double taxation relief, if so, its quantum. India does not have any Double Taxation Avoidance Agreement with countries X and Y.

Solution: (a) Computation of Total Income

Particulars	₹	₹
(a) Income from business:		
(i) Income from profession	3,00,000	
(ii) Share income in partnership firm in country X	2,00,000	5,00,000
(b) Income from other sources:		
(i) Interest from schedule bank	20,000	
(ii) Commission earned in country Y, assumed from other sources	40,000	60,000
Total income		5,60,000
(b) Computation of tax liability :		
Tax on total income of ₹ 5,60,000		46,000
Add : Education cess @ 2%		920
Add : SHEC @		460
		47,380
Less : Double taxation relief : (2,00,000 + 40,000) = 2,40,000 × 8.46%		20,304
Tax payable		27,076
Tax payable to be rounded off to the nearest multiple of ₹ 10 (Sec. 288B)		27,080

Note: (i) Average rate of tax in the foreign country 20%.

(ii) Average rate of tax in India:

$$\frac{47,380}{5,60,000} \times 100 = 8.46\%$$

Whichever is less, is applicable

Illustration 2. Mr. Prasad, ordinarily resident in India, furnished the following particulars of his income/savings during the previous year 2011-2012.

	₹
(i) Income from foreign business (Including ₹ 2,00,000 from business connection in India) accruing outside India	12,00,000
(ii) Loss from Indian business	(-) 2,00,000
(iii) Income from house property	4,00,000
(iv) Dividends gross from Indian companies	60,000
(v) Deposit in Public Provident Fund	70,000
(vi) Tax paid in foreign country	2,50,000
There is no double taxation avoidance treaty. Compute the tax liability	

Solution: (a) Computation of Total Income for the A.Y. 2012-13 :

Particulars	₹	₹
1. Income from House Property		4,00,000
2. Income from Business :		
(a) Income from Indian business	(-) 2,00,000	
(b) (i) Income from foreign business accruing or arising outside India	(+) 10,00,000	
(ii) Income from foreign business deemed to accrue or arise in India	(+) 2,00,000	10,00,000
3. Income from other sources		
Dividends from Indian companies exempt [Sec. 10(34)]		Nil
Gross Total Income		14,00,000
Less : Deduction for approved savings (Sec. 80C): PPF Deposits		70,000
Total Income		13,30,000
Tax liability on total income :		
Income-tax on slab rates		3,48,000
Add: Surcharge on income tax (assuming total income less than one crore)		Nil
Add : Education cess : 2% on the aggregate of income tax and surcharge		6,960
Add : SHEC @ 1%		3,480
Tax liability		3,58,440
Less : Double taxation relief on foreign business profits, not deemed to accrue or arise in India (Sec. 91) 10,00,000 × 20.833%		2,08,330
Tax Payable		1,50,110

Note: 1. Relief is allowed on the doubly taxed income either at average rate of Indian tax or average rate of foreign income tax, whichever is lower;

(a) Average rate of Indian income tax : $3,58,440 / 13,30,000 \times 100 = 26.95\%$

(b) Average rate of foreign income tax : $(2,50,000 / 12,00,000) \times 100 = 20.833\%$



2. The amount of doubly taxed income has been worked out as under:

Income from foreign business, accruing outside India	₹ 12,00,000
Less: (i) Income from business connection deemed to accrue or arise in India which is not entitled to double taxation relief.	2,00,000
Doubly taxed income	10,00,000
 3. Loss from Indian business has been set-off against profits from foreign business which is deemed to accrue or arise in India.
- The mode of set-off increases the amount of double taxation relief.

Illustration 3. The Income-tax Act, 1961 provides for taxation of a certain income earned by X. The Double Taxation Avoidance Agreement, which applies to X, excludes the income earned by X from the purview of tax. Is X liable to pay tax on the income earned by him? Discuss.

Answer : Where any conflict arises between the provisions of the Double Taxation Avoidance Agreement and the Income-tax Act, 1961, the provisions of the Double Taxation Avoidance Agreement would prevail over those of the Income-tax Act. X is, therefore, not liable to pay tax on the income earned by him.

Illustration 4. Explain briefly the proposition of law in case of any conflict between the provisions of the Double Taxation Avoidance Agreement (DTAA) and the Income-tax Act, 1961.

Answer : Where there is conflict between the provision as contained in the tax treaty and the provisions of Income Tax Act, a payer can take advantage of those provisions which are more beneficial to him. Thus, tax treaties override the provisions of Income Tax Act which can be enforced by the appellate authorities/courts.

Illustration 5. Arif, a resident both in India and Malaysia in previous year 2011-2012, owns immovable properties (including residential house) at Malaysia and India. He has earned income of ₹ 50 lakh from rubber estates in Malaysia during the previous year 2011-2012. He also sold some property in Malaysia resulting in short-term capital gain of ₹ 10 lakh during the year. Arif has no permanent establishment of business in India. However, he has derived rental income of ₹ 6 lakh from property let out in India and he has a house in Lucknow where he stays during his visit to India. The Article 4 of the Double Taxation Avoidance agreement between India and Malaysia provides that where an individual is a resident of both the contracting States, he shall be deemed to be resident of the Contracting State in which he has permanent home available to him. If he has permanent home in both the Contracting States, he shall be deemed to be a resident of the Contracting State with which his personal and economic relations are closer (centre of vital interests).

You are required to state with reasons whether the business income of Arif arising in Malaysia and the capital gains in respect of sale of the property situated in Malaysia can be taxed in India.

Answer : Where the Central Government has entered into an agreement with the government of any other country for granting relief to tax or for avoidance of double taxation, the provisions of the Income-tax Act, 1961 are applicable in such case to the extent they are more beneficial to the assessee.

Arif has a residential house both in Malaysia and India. Thus, he has a permanent home in both the countries. However, he has no permanent establishment of business in India. The Double Taxation Avoidance Agreement (DTAA) with Malaysia provides that where an individual is a resident of both countries, he is deemed to be resident of that country in which he has a permanent home and if he has a permanent home in both the countries, he is deemed to be resident of that country, which is the centre of his vital interests, i.e. the country with which he has closer personal and economic relations. Arif owns rubber estates in Malaysia from which he derives business income. However, Arif has no permanent establishment of his business in India. Therefore, his personal and economic relations with Malaysia are closer, since Malaysia is the place where—(a) the property is located and (b) the permanent establishment (PE) has been set-up. Therefore, he is deemed to be resident of Malaysia for AY 2012-2013.

So, in this case, Arif is not liable to income tax in India for assessment year 2012-2013 in respect of business income and capital gains arising in Malaysia.

Illustration 6. Ms. Sania, a resident Indian, furnishes the details for the assessment year 2012-2013 :

	₹
(1) Income from profession	1,04,000
(2) Share income from a partnership in country X (Tax paid in country X for this income in equivalent Indian rupees ₹ 8,000)	40,000
(3) Commission income from concern in country Y (Tax paid in country Y at 20% converted in Indian rupee)	30,000
(4) Interest from scheduled banks	20,000

Ms. Sania wishes to know whether she is eligible to any double taxation relief, if so, its quantum. India does not have any Double Taxation Avoidance Agreement with countries X and Y.

Solution : (a) Computation of Total Income for the A.Y. 2012-13 :

Particulars	₹	₹
(a) Income from Business or Profession :		
(i) Income from Profession	1,04,000	
(ii) Share income in partnership firm in country X	40,000	1,44,000
(b) Income from other sources:		
(i) Interest from schedule bank	20,000	
(ii) Commission earned in country Y, assumed from other sources	30,000	50,000
Total Income		1,94,000

(b) Computation of Tax Liability

Particulars	₹
Tax on Total Income of ₹ 1,94,000	400
Add: Surcharge on income tax	Nil
Education cess @ 2%	400
SHEC @ 1%	8
	4
	412
Less: Double taxation relief : $70,000 \times 0.21\%$	147
Tax payable	265
Rounded off u/s 288B	270
Note: (i) Average rate of tax in the foreign country : 20%	
(ii) Average rate of tax in India : $\frac{412}{194000} \times 100 = 0.21\%$	

Illustration 7. Mr. B is a musician deriving income from foreign concerts performed outside India, ₹ 50,000. Tax of ₹ 10,000 was deducted at source in the country where the concerts were given. India does not have any agreement with that country for avoidance of double taxation. Assuming that Indian income of B is ₹ 2,00,000, what is the relief due to him under Sec. 91 for the assessment year 2012-2013.

Solution :

Computation of Total Income for the A.Y. 2012-13

(a) Computation of Total Income:	₹
(i) Indian Income	2,00,000
(ii) Foreign Income	50,000
Gross Total Income or Total Income	2,50,000
(b) Computation of Tax Liability :	
Income tax on total income :	7,000
Add :	
(i) Education cess @ 2%	140
(ii) SHEC @ 1%	70
	7,210
Less : Double taxation relief under Sec. 91: ₹ 50,000 × 2.884%	1,442
Tax payable	5,768

Note: 1. Average rate of Indian income tax : $= \frac{7,210}{2,50,000} \times 100 = 2.884\%$

2. Average rate of foreign income tax:

Relief is allowed either at the average rate of Indian income tax or the average rate of foreign income tax,

$$\frac{10,000}{50,000} \times 100 = 20\%$$

whichever is lower. Accordingly, the relief has been allowed at the average rate of Indian income tax.

Illustration 8. A resident assessee, earned foreign exchange of ₹ 78,800. The foreign income was also subjected to tax deduction of ₹ 8,800 at source in the foreign country with which India had no agreement for avoidance of double taxation. The assessee claimed relief under Sec. 91 of the Income-tax Act in respect of the whole foreign income. Discuss his contention with reference to decided case laws.

Answer: Where any income is taxed outside India as well as in India, a resident assessee is entitled to claim double taxation relief on such doubly taxed income provided such income is not deemed to accrue or arise in India. If any income arising outside India, is not subjected to tax in India, such foreign income does not form part of doubly taxed income for the purposes of Sec. 91. The expression “doubly taxed income” refers to foreign income which also suffered tax in India.

Where any foreign income, taxed outside India, is also eligible to deduction in computing total income in India, double taxation relief would be allowed only on such income as forms part of total income.

Double taxation relief will be allowed on such doubly taxed income either at the average rate of foreign income tax or Indian income tax, whichever is lower out of the two.

STUDY NOTE - 29

WEALTH TAX

This Study Note includes

- Introduction
- Valuation of Assets
- Other Issues relating to Wealth Tax
- Practical Problems

29.1 INTRODUCTION

Wealth tax is not a very important or high revenue tax in view of various exemptions. Wealth tax is a socialistic tax. It is not on income but payable only because a person is wealthy.

Wealth tax is payable on net wealth on 'valuation date'. As per Section 2(q), valuation date is 31st March every year. It is payable by every individual, HUF and company. Tax rate is 1% on amount by which 'net wealth' exceeds ₹ 15 lakhs. No surcharge or education cess is payable.

No wealth-tax is chargeable in respect of net wealth of any company registered under section 25 of the Companies Act, 1956; any co-operative society; any social club; any political party; and a Mutual fund specified under section 10(23D) of the Income-tax Act [section 45]

COMPUTATION OF NET WEALTH

Particulars	₹
Assets specified in Section 2(ea) chargeable in the hands of assessee on the basis of location of the assets and the assessee's nationality and residential status	xxx
Less: Aggregate value of all the debts owed by the assessee on the valuation date incurred in relation to the above said assets	(xxx)
Less: Assets exempt u/s 5	(xxx)
Add: Deemed asset in the assessee's hands u/s 4	xxx
Net Wealth as per Wealth Tax Act	xxx

Rounding off Net Wealth [Section 44C] : The net wealth computed above shall be rounded off to the nearest multiple of one hundred rupees.

Debt should have been incurred in relation to the assets which are included in net wealth of assessee. Only debt owed on date of valuation is deductible.

In case of residents of India, assets outside India (less corresponding debts) are also liable to wealth tax. In case of non-residents and foreign national, only assets located in India including deemed assets less corresponding debts are liable to wealth tax [section 6].

Net wealth in excess of ₹ 30,00,000 is chargeable to wealth-tax @ 1 per cent (on surcharge and education cess).

Assessment year - Assessment year means a period of 12 months commencing from the first day of April every year falling immediately after the valuation date [Section 2(d)].



29.1.1 Assets

Assets are defined in Section 2(ea) as follows.

Guest house, residential house or commercial building - The following are treated as “assets” - (a) Any building or land appurtenant thereto whether used for commercial or residential purposes or for the purpose of guest house (b) A farm house situated within 25 kilometers from the local limits of any municipality (whether known as a municipality, municipal corporation, or by any other name) or a cantonment board [Section 2(ea)(i)]

A residential house *is* not asset, if it is meant exclusively for residential purposes of employee who is in whole-time employment and the gross annual salary of such employee, officer or director is less than ₹ 5,00,000.

Any house (may be residential house or used for commercial purposes) which forms part of stock-in-trade of the assessee is not treated as “asset”.

Any house which the assessee may occupy for the purposes of any business or profession carried on by him is not treated as “asset”.

A residential property which is let out for a minimum period of 300 days in the previous year is not treated as an “asset”.

Any property in the nature of commercial establishments or complex is not treated as an “asset”.

Motor cars - Motor car is an “asset”, but not the following - (a) motor cars used by the assessee in the business of running them on hire (b) motor cars treated as stock-in-trade [Section 2(ea)(ii)]. In the case of a leasing company, motor car is an asset.

Jewellery, bullion, utensils of gold, silver, etc. [Section 2(ea)(iii)] - Jewellery, bullion, furniture, utensils and any other article made wholly or partly of gold, silver, platinum or any other precious metal or any alloy containing one or more of such precious metals are treated as “assets” [Section 2(ea)(ii)]

For this purpose, “jewellery” includes ornaments made of gold, silver, platinum or any other precious metal or any alloy containing one or more of such precious metals, and also precious or semi-precious stones, whether or not set in any furniture, utensils or other article or worked or sewn into any wearing apparel.

Where any of the above assets (*i.e.*, jewellery, bullion, utensils of gold, etc.) is used by an assessee as stock-in-trade, then such asset is not treated as “assets” under section 2(ea)(iii).

Yachts, boats and aircrafts - Yachts, boats and aircrafts (other than those used by the assessee for commercial purposes) are treated as “assets” [Section 2(ea)(iv)]

Urban land - Urban land is an “asset” [Section 2(ea)(v)]

Urban land means land situated in the area which is comprised within the jurisdiction of a municipality and which has a population of not less than 10,000 according to the last preceding census.

Land occupied by any building which has been constructed with the approval of the appropriate authority is not ‘asset’.

Any unused land held by the assessee for industrial purposes for a period of 2 years from the date of its acquisition by him is not an asset. Any land held by the assessee as stock-in-trade for a period of 10 years from the date of its acquisition by him is also not an asset.

Cash in hand - In case of individual and HUF, cash in hand on the last moment of the valuation date in excess of ₹ 50,000 is an ‘asset’. In case of companies, any amount not recorded in books of account is ‘asset’ [Section 2(ea)(vi)]

29.1.2 Deemed assets

Often, a person transfers his assets in name of others to reduce his liability of wealth tax. To stop such tax avoidance, provision of ‘deemed asset’ has been made. In computing the net wealth of an assessee, the following assets will be included as deemed assets u/s 4.

Assets transferred by one spouse to another - The asset is transferred by an individual after March 31, 1956 to his or her spouse, directly or indirectly, without adequate consideration or not in connection with an agreement to live apart will be ‘deemed asset’ [Section 4(1)(a)(i)]

If an asset is transferred by an individual to his/her spouse, under an agreement to live apart, the provisions of section 4(1)(a)(i) are not applicable. The expression “to live apart” is of wider connotation and even the voluntary agreements to live apart will fall within the exceptions of this sub-clause.

Assets held by minor child - In computing the net wealth of an individual, there shall be included the value of assets which on the valuation date are held by a minor child (including step child/adopted child but not being a married daughter) of such individual [Section 4(1)(a)(ii)]

The net wealth of minor child will be included in the net wealth of that parent whose net wealth [excluding the assets of minor child so includible under section 4(1)] is greater.

Assets transferred to a person or an association of persons - An asset transferred by an individual after March 31, 1956 to a person or an association of person, directly or indirectly, for the benefit of the transferor, his or her spouse, otherwise than for adequate consideration, is 'deemed asset' of transferor [Section 4(1)(a)(iii)]

Assets transferred under revocable transfers - The asset is transferred by an individual to a person or an association of person after March 31, 1956, under a revocable transfer is 'deemed asset' of transferor [Section 4(1)(a)(iv)]

Assets transferred to son's wife [Section 4(1)(a)(v)] - The asset transferred by an individual after May 31, 1973, to son's wife, directly or indirectly, without adequate consideration will be 'deemed asset' of transferor [Section 4(1)(a)(iv)]

Assets transferred for the benefit of son's wife - If the asset is transferred by an individual after May 31, 1973, to a person or an association of the immediate or deferred benefit of son's wife, whether directly or indirectly, without adequate consideration, it will be treated as 'deemed asset' of the transferor [Section 4(1)(a)(vi)].

Interest of partner- Where the assessee (may or may not be an individual) is a partner in a firm or a member of an association of persons, the value of his interest in the assets of the firm or an association shall be included in the net wealth of the partner/member. For this purpose, interest of partner/member in the firm or association of persons should be determined in the manner laid down in Schedule III to the Wealth-tax Act [Section 4(1)(b)].

Admission of minor to benefits of the partnership firm - If a minor is admitted to the benefits of partnership in a firm, the value of his interest in the firm shall be included in the net wealth of parent of minor in accordance with the provisions of section 4(1)(a)(ii) [see para 546.2]. It will be determined in the manner specified in Schedule III.

Conversion by an individual of his self-acquired property into joint family property - If an individual is a member of a Hindu undivided family and he converts his separate property into property belonging to his Hindu undivided family, or if he transfers his separate property to his Hindu undivided family, directly or indirectly, without adequate consideration, the converted or transferred property shall be deemed to be the property of the individual and the value of such property is includible in his net wealth [Section 4(1A)]

If there was such transfer and if the converted or transferred property becomes the subject-matter of a total or a partial partition among the members of the family, the converted or transferred property or any part thereof, which is received by the spouse of the transferor, is deemed to be the asset of the transferor and is includible in his net wealth.

Gifts by book entries - Where a gift of money from one person to another is made by means of entries in the books of account maintained by the person making the gift, or by an individual, or a Hindu undivided family, or a firm or an association of persons, or a body of individuals with whom he has business connection, the value of such gift will be included in the net wealth of the person making the gifts, unless he proves to the satisfaction of the Wealth-tax Officer that the money had actually been delivered to the other person at the time the entries were made [Section 4(5A)]

Impartible estate - For the purpose of the Wealth-tax Act, the holder of an impartible estate shall be deemed to be the owner of all the properties comprised in the estate [Section 4(6)]

Property held by a member of a housing society - Where the assessee is a member of a co-operative housing society and a building or part thereof is allotted or leased to him, the assessee is deemed to be the owner of such building and the value of such building is includible in computing his net wealth. In determining the value of such building, any outstanding instalments, payable by the assessee to the society towards the costs of such house, are deductible as debt owed by the assessee. The above rules are also applicable if the assessee is a member of a company or an association of persons [Section 4(7)]

Property held by a person in part performance of a contract [Section 4(8)] - A person who is allowed to take or retain possession of any building or part thereof in part performance of a contract of the nature referred to in section 53A of the Transfer of Property Act, 1882. Similarly, a person can acquire any rights, excluding any rights by way of a lease from month to month or for a period not exceeding one year, in or with respect to any building or part thereof, by virtue of transaction as is referred to in section 269UA(f) of the Income-tax Act.



In above cases, the assets are taxable in the hands of beneficial owners, in the same manner in which they are taxed under the Income-tax Act :

29.1.3 Assets which are exempt from tax

The following assets are exempt from wealth-tax, as per section 5.

Property held under a trust - Any property held by an assessee under a trust or other legal obligation for any public purpose of charitable or religious nature in India is totally exempt from tax. [Section 5(i)].

Business assets held in trust, which are exempt - The following business assets held by an assessee under a trust for any public charitable / religious trust are exempt from tax - (a) where the business is carried on by a trust wholly for public religious purposes and the business consists of printing and publication of books or publication of books or the business is of a kind notified by the Central Government in this behalf in the Official Gazette (b) the business is carried on by an institution wholly for charitable purposes and the work in connection with the business is mainly carried on by the beneficiaries of the institution (c) the business is carried on by an institution, fund or trust specified in sections 10(23B) or 20(23C) of the Income-tax Act.

Any other business assets of a public charitable / religious trust is not exempt.

Coparcenary interest in a Hindu undivided family - If the assessee is a member of a Hindu undivided family, his interest in the family property is totally exempt from tax [Section 5(ii)].

Residential building of a former ruler - The value of any one building used for the residence by a former ruler of a princely State is totally exempt from tax [Section 5(iii)]

Former ruler's jewellery - Jewellery in possession of a former ruler of a princely State, not being his personal property which has been recognised as a heirloom is totally exempt from tax [Section 5(iv)]

The jewellery shall be permanently kept in India and shall not be removed outside India except for a purpose and period approved by the Board. Reasonable steps shall be taken for keeping that jewellery substantially in its original shape. Reasonable facilities shall be allowed to any officer of the Government, or authorised by the Board, to examine the jewellery as and when necessary.

Assets belonging to the Indian repatriates - Assets (as given below) belonging to assessee who is a person of Indian origin or a citizen of India, who was ordinarily residing in a foreign country and who has returned to India with intention to permanently reside in India, is exempt. A person shall be deemed to be of Indian origin if he, or either of his parents or any of his grand-parents, was born in undivided India.

After his return to India, following shall not be chargeable to tax for seven successive assessment years - (a) moneys brought by him into India (b) value of asset brought by him into India (c) moneys standing to the credit of such person in a Non-resident (External) Account in any bank in India on the date of his return to India and (d) value of assets acquired by him out of money referred to in (a) and (c) above within one year prior to the date of his return and at any time thereafter [Section 5(v)]

One house or part of a house - In the case of an individual or a Hindu undivided family, a house or a part of house, or a plot of land not exceeding 500 sq. meters in area is exempt. A house is qualified for exemption, regardless of the fact whether the house is self-occupied or let out. In case a house is owned by more than one person, exemption is available to each co-owner of the house [Section 5(vi)]

29.2 VALUATION OF ASSETS

The value of an asset, other than cash, shall be its value as on the valuation date determined in the manner laid down in Schedule III.

Valuation of a building - Value of any building or land appurtenant thereto, or part thereof, is to be made in accordance with Part B of Schedule III to the Wealth-tax Act

The first step is to find out gross maintainable rent. Gross maintainable rent is (a) annual rent received / receivable by the owner or annual value of the property as assessed by local authority, whichever is higher (if the property is let out) or (b) annual rent assessed by the local authority or if the property is situated outside the jurisdiction of a

local authority, the amount which the owner can reasonably be expected to receive as annual rent had such property been let (if the property is not let).

In the following cases “actual rent” shall be increased in the manner specified below : (a) Taxes borne by tenant (b) If property is rented, one-ninth of actual rent will be added, if expenditure on repairs in respect of the property is borne by the tenant (c) Interest @ 15% on deposit given by tenant or difference (d) Premium received as consideration for leasing of the property or any modification of the terms of the lease will be divided over the number of years of the period of the lease and will be added to ‘actual rent’ (d) If the derives any benefit or perquisite as consideration for leasing of the property or any modification of the terms of the lease), the value of such benefit or perquisite shall be added to actual rent.

Net maintainable rent is determined by deducting from the gross maintainable rent (a) the amount of taxes levied by any local authority in respect of property (deduction is available even if these are to be borne by the tenant) ; and (b) A sum equal to 15% of gross maintainable rent.

The net maintainable rent is finally capitalized to arrive as value of net asset.. This can be done by multiplying the net maintainable rent by 12.5. If the property is constructed on leasehold land, net maintainable rent is to be multiplied by 10 when the unexpired period of lease of such land is 50 years or more and multiplied by 8 where the unexpired period of lease of such land is less than 50 years).

If a property is acquired/constructed after March 31, 1974, then the value of the house property is determined as above. Original cost of construction/acquisition *plus* cost of improvement of the house property is calculated. The higher of the above is taken as capitalised value of net maintainable rent. This exception is applicable in respect one house property. The cost of acquisition/construction (*plus* cost of improvement) does not exceed ₹ 50 lakh, if the house is situated at Bombay, Calcutta, Delhi and Madras (₹ 25 lakh at any other place).

If unbuilt area of the plot of land on which the property is built exceeds the specified area, premium is to be added to the capitalised value determined above.

Valuation of self-occupied property - If assessee owns a house (or a part of the house), being an independent residential unit and is used by the assessee exclusively for his residential purposes throughout 12 months ending on the valuation date, valuation will be as per provisions of section 7(2).

Assessee can either take value of the house as determined above on the valuation date relevant for the current assessment year or he take value of the house, as determined above, on the first valuation date next following the date on which he became the owner or the valuation relevant for the assessment year 1971-72, whichever is later. The choice is of the assessee.

Where the house has been constructed by the assessee, he shall be deemed to have become the owner thereof on the date on which the construction of such house was completed.

Valuation of assets of business - If the assessee is carrying on a business for which accounts are maintained by him regularly, the net value of the assets of the business as a whole, having regard to the balance sheet of such business on the valuation date, is taken as value of such assets [Part D, Schedule III].

- (A) The assets are valued as follows - **Depreciable assets** - Written down value, plus 20%, **Non-depreciable assets (other than stock-in- trade)** - Book value, plus 20%, **Closing stock** - Value adopted for the purpose of income-tax, plus 20%.
- (B) Then value of house property, life interest, jewellery and other assets is calculated as per other provisions of Wealth Tax Act.

Higher of A or B is taken as value of assets.

Value of interest in firm or association of persons - The net wealth of the firm on the valuation date is ascertained.. For determining the net wealth of the firm (or association), no account shall be taken of the exemptions given by section 5. The portion of the net wealth as is equal to the amount of the capital of the firm or association is allocated amongst the partners or the members in the proportion in which capital has been contributed by them.

The residue of the net wealth is allocated amongst the partners or the members in accordance with the agreement of the partnership or association of persons for the distribution of assets in the event of dissolution of the firm or association or in the absence of such agreement, in the proportion in which the partners (or members) are entitled to share profits [Part E, Schedule III]



Value of life interest - The value of life interest of an assessee shall be determined as per Part F, Schedule III. Average net annual income of the assessee derived from the life interest during 3 years ending on the valuation date is calculated. While computing net annual income, expenses incurred on the collection of such income (maximum of 5% of the average of annual gross income) shall be deducted. This is multiplied as per formula prescribed to arrive at value of asset.

Valuation of jewellery - The value of jewellery shall be estimated to be the price which it would fetch if sold in the open market on the valuation date (*i.e.*, fair market value). Where the value of jewellery does not exceed ₹ 5,00,000, a statement in Form No. O-8A is to be submitted. Where the value of the jewellery exceeds ₹ 5,00,000, a report of a registered valuer in Form No. O-8 should be submitted. The report is not binding on assessing officer (Valuation Officer) and he can determine fair market value of jewellery.

The value of jewellery determined by the Valuation Officer for any assessment year shall be taken to be the value of such jewellery for the subsequent four assessment years subject to the prescribed adjustments.

Valuation of any other asset - The value of any asset, other than cash (being an asset which is not covered in above paras) shall be estimated either by the Assessing Officer himself or by the Valuation Officer if reference is made to him under section 16A. In both these cases, the value shall be estimated to be the price which it would fetch if sold in the open market, on the valuation date. If the asset is not saleable in the open market, the value shall be determined in accordance with guidelines or principles specified by the Board from time to time by general or special order.

29.3 OTHER ISSUES RELATING TO WEALTH TAX

Charitable or religious trusts - A trust can forfeit exemption for any of the following reasons - (a) any part of the trust's property or any income of the trust, including income by way of voluntary contributions, is used for the benefit of the settlor, the trustee, their relatives etc.; or (b) any part of the income of the trust, created on or after April 1, 1962, including income by way of voluntary contributions, enures directly or indirectly, for the benefit of any of the persons referred to in section 13(3) of the Income-tax Act; or (c) any funds of the trust are invested or deposited or any shares in a company are held by the trust in contravention of the investment pattern for trust funds laid down in section 11(5) of the Income-tax Act.

In such case, tax shall be leviable upon and recoverable from the trustee or manager in respect of the property held by him under trust at the rate of tax applicable to a resident in India.

These provisions are not applicable in the case of a scientific research association [Section 10(21) of the Income-tax Act] and in the case of any institution, fund or trust referred to in section 10(22), (22A), (22B) or (23C) of the Income-tax Act in specified situations [Section 21A]

Association of persons where shares of members are indeterminate/unknown - If assets chargeable to wealth-tax are held by an association of persons and the individual shares of the members in the income or assets of the association are indeterminate or unknown, wealth-tax is levied to the same extent as it would be leviable upon and recoverable from an individual who is citizen of India and resident in India [Section 21AA]

29.3.1 Return of wealth and assessment

Every person is required to file with the Wealth-tax Officer a return of net wealth in Form BA, if his net wealth or net wealth of any other person in respect of which he is assessable under the Act on the valuation date is of such an amount as to render him liable to wealth-tax. Return can be filed on or before the "due date" specified under section 139 of the Income-tax Act.

Return in response to a notice - In the case of any person who, in the opinion of Wealth-tax Officer, is assessable to tax, the Wealth-tax Officer may, before the end of the relevant assessment year, issue a notice requiring him to furnish, within 30 days from the date of service of such notice, a return of net wealth in the prescribed form.

Assessment - The assessee is required to pay the tax before filing of the return and such return is to be accompanied by the proof of such payment. Provisions of regular assessment, as applicable under Income Tax, will apply to wealth tax also.

Interest or penalty and prosecution - Interest @ 1% per month is payable for failure to pay wealth tax on due date. Penalty and prosecution provisions also apply.

29.4 PRACTICAL PROBLEMS

Illustration 1.

ALtd is engaged in the construction of residential flats. For the valuation date 31.3.2012, it furnishes the following data and requests you to compute the taxable wealth -

- Land in urban area (Construction is not permitted as per Municipal Laws in force) ₹ 55,00,000
- Motor-cars (used on hire by the company) ₹ 10,00,000
- Jewellery (Investment) ₹ 25,00,000. Loan taken for purchasing the same ₹ 20,00,000
- Cash Balance (as per books) ₹ 2,75,000
- Bank Balances ₹ 5,50,000
- Guest House (situated in a place which is 30 Kms away from the local limits of the municipality) ₹ 10,00,000
- Residential flats occupied by the Managing Director ₹ 15,00,000. The Managing Director is on whole time appointment and is drawing remuneration of ₹ 2,00,000 per month.
- Residential house were let out on hire for 200 days ₹ 10,00,000

Solution :

The computation should be supported with proper reasoning for inclusion or exclusion.

Valuation Date: 31.03.2012 Computation of Taxable Wealth

Nature of asset	₹	Reason
Land in Urban Area	NIL	Land in which construction is not permitted as per municipal law is not an asset u/s 2(ea)
Motor Cars	NIL	Motor cars used in business of hire is not an asset u/s 2(ea)
Jewellery	25,00,000	Not held as stock in trade
Cash Balance	NIL	Cash as per books - Not an asset U/s 2(ea)
Bank Balance	NIL	Not an asset u/s 2(ea)
Guest House	10,00,000	Asset u/s 2(ea)
Residential Flat occupied by MD	15,00,000	Asset u/s 2(ea) since Annual Gross Salary is greater than ₹5,00,000.
Residential House Let-out	10,00,000	Asset U/s 2(ea) as it is not let-out for a period - 300 days.
Total Assets		
Less: Debt incurred in relation to an asset: Loan for Jewellery	60,00,000 (20,00,000)	
Taxable Net Wealth	40,00,000	
Less : Basic Exemption	30,00,000	
Taxable Net Wealth	10,00,00	
Tax Payable @1%	10,000	

Illustration 2. Samir furnishes the following particulars for the compilation of his Wealth Tax return for Assessment Year 2012-13.

- Gifts of jewellery made to wife from time to time aggregating ₹80,000. Market value on valuation date ₹3,00,000
- Flat purchased under installment payment scheme in 1979 for ₹9,50,000. Used for purposes of his residence and market value as on 31.3.2011. (Installment remaining unpaid ₹ 80,000) ₹10,00,000
- Urban land transferred to minor handicapped child valued on 31.3.2011 ₹5,00,000.

Solution : Explain how you will deal with these items. Make suitable assumptions if required.

Particulars	Taxable	Reasons
Gift of Jewellery made to wife	₹ 3,00,000	Deemed asset u/s 4. Fair Market Value of the Jewellery is taxable.
Flat used for residence	NIL	Taxable as an asset u/s 2(ea) but the assessee can claim exemption u/s 5(vi). So full value of the asset is exempt from tax.
Urban Plot in the hands of the minor	NIL	Asset held by the minor who is handicapped u/s 80U, clubbing provisions does not apply.

Illustration 3. Compute the net wealth of Nivedita, a resident individual as on 31.3.2012 from the following particulars furnished —

- She has a house property at Delhi, valued at ₹ 20,00,000 which is occupied by a firm in which she is a partner for its business purposes. Another house at Mumbai, valued at ₹ 8,00,000 is being used for his own business.
- Vehicles for personal use - (i) Motor Car ₹ 10,00,000 (ii) Motor Van — ₹ 3,00,000 (iii) Jeep — ₹ 5,00,000.
- Cash on hand - ₹ 3,10,000
- Jewellery - ₹ 10,00,000
- Nivedita has gifted to a Trust a residential property situated at Kolkata purchased 5 years back for ₹ 20,00,000 for the benefit of the smaller HUF consisting of herself and her spouse and let-out for 8 months. Schedule-III, Rule 3 value as on 31.3.2010 is ₹ 14 Lakhs.
- She had transferred an urban house plot in February 1999 in favour of her niece which was not revocable during her life time. This niece died on 14.3.2009. Nivedita could get the title to the plot retransferred to her name only on 15.4.2009 despite sincere and honest efforts. The market value of the house as on 31.3.2012 is ₹ 10,00,000.
- Nivedita is the holder of an impartible estate in which urban agricultural lands of the value of ₹ 4,30,000 as on 31.3.2012 are comprised.

Solution :

Assessee: Ms. Nivedita Valuation Date: 31.3.2012 Assessment Year: 2012-13

Computation of Net Wealth

Nature of Asset	Amount Taxable	Reasons
House Property at Delhi used for business by a firm in which he is a partner	NIL	Property used for business purpose is not an asset u/s 2(ea) (Refer Note)
House Property at Mumbai used for his own business	NIL	Property used for business purpose is not an asset u/s 2(ea)
Vehicles for Personal Use		
1. Motor-car	10,00,000	Vehicles used for personal purposes are assets u/2(ea)
2. Motor-van	3,00,000	
3. Jeep	5,00,000	
Cash on Hand	2,60,000	For an Individual, cash in excess of ₹ 50,000 shall be chargeable to Wealth Tax u/s 2(ea) (₹3,10,000 - ₹50,000)
Jewellery	10,00,000	Jewellery other than those held as stock-in-trade are asset u/s 2(ea)

Contd...

Property at Kolkata transferred to a Trust 20,00,000	NIL	Taxable u/s 4(1A). Value = Higher of Value as on Valuation Date ₹14 Lakhs or Cost of Acquisition ₹ 20 Lakhs
Less: Exemption u/s 5(vi) 20,00,000		
Urban House Plot transferred to Niece	10,00,000	Taxable u/s 4(5) as the title to the property stands vested in Nivedita's hands immediately on niece's demise
Urban Agricultural Land	4,30,000	Holder of an impartible estate is deemed to be the owner of all properties comprised therein u/s 4(6)
NET WEALTH	44,90,000	
Less : Basic Exemption	30,00,000	
Taxable Net Wealth	14,90,000	
Taxable Payable @ 1%	14,900	

Illustration 4. SIPRA Constructions Ltd. is engaged in the construction of residential flats. For the valuation date 31.3.2012, furnishes the following data and requests you to compute the taxable wealth:

- Land in urban area (construction is not permitted as per Municipal laws in force) ₹ 50 lakhs
- Motor-cars (in the use of company) ₹10lakhs
- Jewellery (Investment) ₹10 lakhs
- Cash balance (As per books) ₹ 3 lakhs
- Bank Balance (As per books) ₹ 6 lakhs
- Guest House (Situated in rural area) ₹ 8 lakhs
- Residential flat occupied by Managing Director (Annual remuneration of whom is ₹8 Lakhs excluding perquisites) ₹ 10 lakhs
- Residential house let-out for 100 days in the financial year ₹ 5 lakhs
- Loan obtained for :
 - Purchase of Motor Car ₹ 3 lakhs
 - Purchase of Jewellery ₹ 2 lakhs

Solution :

Assessee: SIPRA Constructions Ltd. Valuation Date: 31.3.2012 Assessment Year: 2012-13

Nature of Asset	Amount taxable (₹ Lakhs)	Reasons
Land in Urban Area	NIL	Land in which construction is not permitted as per municipal laws is not an asset u/s 2(ea)
Motor-cars	10	Motor-car other than those used in the business of hire or held as stock-in-trade is an asset u/s 2(ea)
Jewellery	10	Not held as stock-in-trade - asset u/s 2(ea)
Cash Balance	NIL	Cash as per books - not an asset u/s 2(ea)
Bank Balance	NIL	Not an asset u/s 2(ea)
Guest House	8	Asset u/s 2(ea)
Residential Flat Occupied by MD	10	Asset u/s 2(ea)-since Gross Annual Salary of Managing Director is greater than ₹ 5 Lakhs
Let-out Residential House Property	5	Asset u/s 2(ea) - since not let-out for a period exceeding 300 days
TOTAL ASSETS	43	
Less: Debt incurred in relation to Assets		
1. Purchase of Motor-car	(3)	
2. Purchase of Jewellery	(2)	
NET WEALTH	38	
Less : Basic Exemption	30	
Taxable Net Wealth	8	
Taxa Payable @ 1%	8,000	

Illustration 5. Sunrise Promoters & Developers Ltd. a widely held company owns the following assets as on 31.3.2012 : -

- Land at Rajarhat (West Bengal) purchased in 2002 on which a residential complex consisting of 24 flats, to be sold on ownership basis, is under construction for last 18 months
- Two office flats at Noida purchased for resale in the year 2003
- Shares of Group Companies, break-up value of which is ₹ 19,00,000
- Cash at construction site ₹ 8,00,000
- Residential flat in occupation of company's whole-time director drawing a salary of ₹4,50,000 per annum.

Which of the above assets will be liable for wealth? Give reasons in brief.

Solution : **Assessee: Sunrise Promoters & Developers Ltd. Valuation Date: 31.3.2012**
Assessment Year: 2012-13

Nature of Asset	Amount Taxable	Reasons
Land at Rajarhat purchased in 2005	NIL	Urban Land held as stock-in-trade for a period less than 10 Years -not an asset u/s 2(ea)
Residential Flats at Noida purchased in 2004 for resale	NIL	House Property held as stock-in-trade - not an asset u/s 2(ea)
Shares of Group Companies	NIL	Not an asset u/s 2(ea)
Cash at construction site	NIL	Any amount recorded in the books of account is not an asset u/s 2(ea)
Residential House Property for Whole-Time Director	NIL	Since Gross Annual Salary of Whole Time Director is less than ₹ 5 Lakhs - not an asset u/s 2(ea)

Illustration 6. Hassan, a person of Indian origin was working in Australia since 1986. He returned to India for permanent settlement in June 2004 when he remitted the moneys into India. He furnished the following particulars of his wealth as on 31.3.2012. You are required to arrive at his wealth in respect of Assessment Year 2012-13 :

- Market Value of Residential house in Jharkhand (let-out for residence) ₹ 10,00,000 with Net Maintainable Rent p.a. of ₹ 1,20,000.
- Share in building owned by a firm in which Hassan is a Partner - used for business ₹ 5,00,000
- Motor-car purchased in April 2009, out of moneys remitted to India from Australia ₹ 4,00,000
- Value of interest in Firm excluding item (b) above ₹ 5,00,000
- Shares in companies (quoted) ₹ 2,00,000
- Assets purchased out of amount remitted from Australia :
 - Jewellery purchased in March 2002 ₹ 5,50,000
 - Vacant land purchased in October 2000 ₹ 10,00,000
- Amount standing to the credit of NRE Account ₹ 15,00,000
- Cash on hand (out of sale proceeds of agricultural income) ₹ 65,000

Solution : **Assessee: Hassan Valuation Date: 31.3.2012 Computation of Net Wealth**

Nature of Asset	Amount Taxable	Reasons
Residential House in Jharkhand	NIL	Not an Asset u/s 2(ea) - Let-out for whole year -Hence, not taxable
Share in the building owned by the firm	NIL	Not an asset u/s 2(ea), used for its own business - not chargeable to tax
Motor-car 4,00,000		
Less: Exempt u/s 5(v)-acquired out of money brought into India (4,00,000)	NIL	Asset u/s 2(ea). But, exemption available u/s 5(v), since acquisition out of money brought into India.
Value of Interest in a Firm	5,00,000	Assumed as deemed asset u/s 4(1)(b)
Shares in Companies	NIL	Not an asset u/s 2(ea)
Value of Jewellery	5,50,000	Asset u/s 2(ea) - Not entitled for exemption
Vacant Land	10,00,000	Asset u/s 2(ea) - Purchased in October 2000
Money in NRE A/c	NIL	Not an asset u/s 2(ea)
Cash in Hand in excess of ₹ 50,000	15,000	Asset u/s 2(ea), being an Individual
NET WEALTH	20,65,000	
Tax Liability	Nil	

Since less than the Basic Exemption limit.

Illustration 7. Romit Roy, a Not Ordinarily Resident in India seeks your advice with regard to the furnishing of his Wealth Tax Return. The value of assets held on 31.3.2012 is indicated below. You are requested to compute the Taxable Wealth.

- Motor cars of foreign make held as Fixed Assets ₹26 lakhs
- Gold bonds under Gold Deposit Scheme, 2000 ₹25 lakhs
- Residential House Property at Kolkata let out w.e.f.10.2.2011 ₹30 lakhs
- Jewellery held ₹20 lakhs
- Lands purchased for industrial purpose: (a) on 1.1.2005 ₹ 7 lakhs (b) on 24.2.2011 ₹10 lakhs
- Loans against the purchase of land : (a) on 1.1.2006 ₹ 4 lakhs (b) on 24.2.2011 ₹5 lakhs
- Fixed Assets located in Abu Dhabi ₹ 80 lakhs
- Cash at Bank ₹4 lakhs
- Cash in Hand ₹ 80,000
- Mrs. Roy acquired out of gifts received from her husband:

(a) Shares and securities ₹3,00,000

(b) Residential House property at Bangalore ₹20,00,000

Solution : **Assessee: Romit Roy**

Valuation Date: 31.3.2012

Assessment Year: 2012-13

Computation of Taxable Wealth

Nature of Asset	₹	Reasons
Motor-cars	26,00,000	Motor-car other than those used in the business of hire or held as stock-in-trade is an asset u/s 2(ea)
Gold Bonds, 1999	Nil	Not an asset under WT Act.
Residential House Property	Nil	Any residential house property let-out for 300 days or more is not an asset
Jewellery	20,00,000	Jewellery other than those held as stock-in-trade is an asset
Land purchased on 1.1.05 for Industrial Purpose	7,00,000	Land held beyond two years from the date of acquisition for industrial purposes is an asset
Land purchased 24.2.2010	Nil	Land held for first two years from the date of acquisition for industrial purposes is not an asset
Cash-on-Hand	30,000	Cash held beyond ₹ 50,000 is an asset
Cash-at-Bank	Nil	Not an asset under WT Act.
Fixed Asset located in Abu Dhabi	Nil	Not chargeable to tax for Not Ordinary Resident
Deemed Assets acquired and held by Mrs.Roy		
(a) Shares and Securities	Nil	Not an asset u/s 2(ea)
(b) Res.House Property at Bangalore		Asset u/s 2(ea).
20,00,000		
Less: Exemption u/s 5(vi) (20,00,000)	Nil	One house or part of the house exempt u/s 5(vi)
Total Assets	53,30,000	
Less: Debts incurred on Taxable Assets		Wealth Tax Liability and Debts incurred in relation to exempted assets are not deductible
On Land acquired on 1.1.2006	(4,00,000)	
Net Wealth	49,30,000	
Less: Basic Exemption	30,00,000	
Taxable Wealth	19,30,000	
Tax Payable @ 1%	19,300	

VALUATION OF IMMOVABLE PROPERTY

Illustration 8. Abhishek, a person of Indian origin was working in Austria since 1991. He returned to India for permanent settlement in May 2011 when he remitted money into India. For the valuation date 31.3.2012, the following particulars were furnished. You are required to compute the taxable wealth. The reason for inclusion or exclusion should be stated –

- Building owned and let-out for 270 days for residence. Net maintainable rent (₹1,00,000) and the Market Value (Excess of Unbuilt Area over Specified Area is 20% of the Aggregate Area) ₹ 30 lakhs
- Jewellery : (a) Purchased in April 2011 out of money remitted to India from Austria ₹12,00,000
(b) Purchased in May 2011 out of sale proceeds of motor-car brought from abroad and sold for ₹ 40 lakhs.
- Value of interest in urban land held by a firm in which he is a partner ₹10 lakhs
- Bonds held in companies ₹10 lakhs
- Motor car used for own business ₹ 25 lakhs
- Vacant house plot of 480 sq. mts. (purchased in December 2003) market value of ₹ 20,00,000
- Cash in hand ₹ 45,000
- Urban land purchased in the year 2008 out of withdrawals of NRE Account ₹ 15,00,000

Solution :

Assessee : Abhishek Valuation Date : 31.3.2012 Assessment Year : 2012-13

Computation of Net Wealth

Nature of the Asset	₹	₹	Reasons
Value of the House		18,50,000	Asset u/s 2(ea). Working Note 1
Jewellery: Purchased in April 2011	12,00,000		Asset u/s 2(ea).
Less: Exempt u/s 5(v)	(12,00,000)	Nil	Purchased out of money brought into India
Jewellery			Asset u/s 2(ea).
Jewellery: Purchased in May 2011	40,00,000		Purchased out of sale proceeds of assets brought into India
Less: Exempt u/s 5(v)	(40,00,000)	Nil	Deemed Asset u/s 4(1)(b)
Interest in Urban Land held by firm		10,00,000	Not an asset u/s 2(ea)
Bonds held in companies	—	Nil	Asset u/s 2(ea). Not held as stock-in-trade
Motor car		25,00,000	Asset u/s 2 (ea)
Vacant House Plot (480 sq. mts.)	20,00,000		House/part of house/plot less than 500 sq.mts.
Less: Exempt u/s 5(vi)	(20,00,000)	Nil	Since not exceeding ₹50,000
Cash in hand		Nil	Purchased out of money brought into India
Urban Land Purchased	15,00,000		
Less: Exempt u/s 5(v)	(15,00,000)	Nil	
NET WEALTH		53,50,000	
<i>Less : Basic Exemption</i>		30,00,000	
Net Taxable Wealth		23,50,000	
Tax Payable @ 1%		23,500	


(1) Working Notes: Valuation of Building :

Net Maintainable Rent(NMR)	= ₹1,00,000
Capitalized Value of NMR=NMR×12.5 (Owner of the land) = ₹ 1,00,000 × 12.5	= ₹12,50,000
Add : Premium for excess of unbuilt area (20%) over specified area = 40% of CNMR	= ₹ 5,00,000
VALUE OF THE HOUSE	₹18,50,000

Illustration 9. Mr. Kushal Sengupta owns a house at Jharkhand, which is let-out at ₹1,35,000 per annum. The annual value of the property as per municipal records also is ₹1,00,000. Municipal taxes are partly borne by the owner (₹5,000) and partly by the tenant (₹6,000). Repair expenses are borne by tenant (₹10,000) the difference between the un-built area and specified area does not exceed 5%. The property was acquired on 10.5.1998 for ₹ 15,00,000.

Determine for purposes of Wealth Tax Act, the value of the property as on 31.3.2012 on the following situations —

- The house is built on a freehold land.
- It is built on a leasehold land, the unexpired period of lease of the land is more than 50 years.
- If the area of the plot on which the house is built is 800 sq. meters. FSI, permissible is 1.4 and FSI utilised is 1088 Sq. metres. (136 Sq. metres × 8 Storeys)
- The tenant had made interest free deposit of ₹ 1,00,000 with the landlord.

Solution :

Assessee : Mr. Kushal Sengupta Valuation Date : 31.3.2012 Assessment Year : 2012-13

Computation of Value of House Property

For Situations (a) & (b):

Computation of Gross Maintainable Rent (Amount in ₹)

Particulars	No Rental Deposit	Rental Deposit excess of 3 Mths
Actual Annual Rent	1,35,000	1,35,000
Add: Municipal Taxes borne by the tenant	6,000	6,000
1/9 th of Actual Rent Receivable since repair expenses are borne by the tenant (₹1,35,000/ 9)	15,000	15,000
Rental Deposits - 15% Interest on ₹ 1,00,000	Nil	15,000
GROSS MAINTAINABLE RENT	1,56,000	1,71,000
Less: Municipal Taxes Paid	11,000	11,000
Less: 15% of Gross Maintainable Rent	23,400	25,650
Net Maintainable Rent	1,90,400	2,07,650
Case (a) Capitalization of Net Maintainable Rent		
-Freehold Land NMR x 12.5	23,80,000	25,56,625
Case (b) Capitalization of Net Maintainable Rent		
-Leasehold Land - Unexpired Lease 50 Years = NMR×10	19,04,000	20,07,650
Property Acquired after 31.3.1974 i.e. 10.5.1997	15,00,000	15,00,000
Therefore, Value of the Property (whether on Lease-hold Land or on Freehold Land)	15,00,000	15,00,000

For Situation (c) : In case of excess unbuilt area :

Unbuilt Area = (Actual Area of the Land less Built up Area) = (800 sq. mt less 136 sq. mt). = 664 sq. mt.

Excess Unbuilt Area = (Unbuilt Area less Specified Area) = 664 sq. mt. less 70% of 800 sq. mt. = 664 Less 560 = 104 sq. mt

% of Excess Unbuilt Area = $\text{Excess Unbuilt Area} \times 100 / \text{Aggregate Area} = 104 \times 100 / 800 = 13\%$

Therefore, Value of the Property = Substituted Net Maintainable Rent i.e. ₹15,00,000 + 30% of SNMR = ₹ 19,50,000

Illustration 10. From the following dated furnished by Mr.Soumitra, determine the value of house property built on leasehold land as at the valuation date 31.3.2012 :

Particulars	₹
Annual Value as per Municipal valuation	1,40,000
Rent received from tenant (Property vacant for 3 months during the year)	1,08,000
Municipal tax paid by tenant	10,000
Repairs on property borne by tenant	8,000
Refundable deposit collected from tenant as security deposit which does not carry any interest	50,000
The difference between unbuilt area and specified area over aggregate area is 10.5%.	

Solution :

Assessee: Mr. Soumitra Valuation Date: 31.3.2011 Assessment Year: 2012-13

Computation of Value of House Property

Step I: Computation of Gross Maintainable Rent(GMR)

Particulars	₹	₹
Actual Annual Rent- ₹ 1,08,000 × 12 Months/9 Months		1,44,000
Add: Municipal tax paid by the Tenant 10,000		
1/9 th of Actual Rent Receivable as repair expenses are borne by the tenant - ₹ 1,44,000/9	16,000	
Interest on Refundable Security Deposit- ₹ 50,000 × 15% × 9/12	6,000	32,000
GROSS MAINTAINABLE RENT (GMR)		1,76,000

Step II: Computation of Net Maintainable Rent (NMR)

Particulars	₹	₹
Gross Maintainable Rent (GMR)		1,76,000
Less: Municipal Taxes levied by the local authority	10,000	
15% of Gross Maintainable Rent - ₹1,76,000 × 15%	26,400	(36,400)
NET MAINTAINABLE RENT (NMR)		1,39,600

Step III: Capitalisation of the Net Maintainable Rent (CNMR) (Assumed that unexpired lease period is more than 50 Years)

NMR × Multiple Factor for an Unexpired Lease Period - ₹ 1,39,600 × 10 = ₹ 13,96,000

Step IV: Addition of Premium to SNMR in case of excess inbuilt area:

Particulars		₹
Add: Capitalisation of the Net Maintainable Asset		13,96,000
Premium for excess of 10.5% unbuilt area over specified area-30% of CNMR		4,18,800
Value of House Property as per Wealth Tax Act		18,14,800

Illustration 11. Property Company Ltd. has let-out a premise with effect from 1.10.2011 on monthly rent of ₹1.5 lakh. The lease is valid for 10 years and the tenant has made a deposit equivalent to 3 months rent. The tenant has undertaken to pay the municipal taxes of the premises amounting to ₹ 2 lakh. What will be the value of the property under Schedule III of the Wealth Tax Act for assessment to wealth tax?

Solution :

Assessee: Property Company Ltd. Valuation Date: 31.3.2012 Assessment Year : 2012-13

Computation of Value of Let-out Property

Actual Annual Rent Receivable - ₹ 1,50,000 × 12 Months	18,00,000
Add: Municipal Taxes borne by the Tenant	2,00,000
GROSS MAINTAINABLE RENT	20,00,000
Less: Municipal Taxes levied by the Municipal Authority	2,00,000
Less: 15% of Gross Maintainable Rent (₹ 20,00,000 × 15%)	3,00,000
NET MAINTAINABLE RENT	15,00,000

Value of the Property = Capitalized Value of NMR

NMR × 8 (unexpired period of lease is less than 50 years) = ₹ 15,00,000 × 8 = ₹ 1,20,00,000

VALUATION OF PARTNER'S INTEREST IN FIRM

Illustration 12. Net wealth of firm consisting of three partners Bidyut, Kingshuk and Deepak in 2:2:1 and a capital contribution of ₹17 Lakhs, ₹13 Lakhs, and ₹12 Lakhs respectively is as under -

(a) Value of assets located outside India	₹ 30,00,000
(b) Value of assets located in India	₹ 80,00,000
(c) Debts incurred in relation to assets in India	₹ 40,00,000

Determine the value of interest of the partners in the firm under the Wealth Tax Act, 1957.

Solution :

**Assesses: Bidyut, Kingshuk & Deepak Valuation Date: 31.3.2012
Assessment Year: 2012-13**

Computation of net wealth of the Firm

Particulars	₹	₹
Value of Assets located in India	80,00,000	
Less: Liability in relation to assets in India	<u>40,00,000</u>	40,00,000
Value of Assets located outside India		30,00,000
Net Wealth of the Firm		70,00,000

Solution :

Computation of Interest of the Partner in the net wealth of the Firm (Amount in ₹)

Particulars	Bidyut	Kingshuk	Deepak
To the extent of Capital Contribution	17,00,000	13,00,000	12,00,000
Balance (Net Wealth-Capital Contribution) in Profit sharing ratio since dissolution ratio is not given	11,20,000	11,20,000	5,60,000
Interest of the Partner in the Net Wealth of the Firm	28,20,000	24,20,000	17,60,000

Computation of the Interest of the Partner in the net wealth of the Firm on the basis of location of assets: (Interest of the Partner in the Firm apportioned in the ratio of 4:3)

Particulars	Balu	Kausik	Deepu
Assets Located Inside India	16,11,429	13,82,857	10,05,714
Assets Located Outside India	12,08,571	10,37,143	7,54,286
Interest of the Partner in the Net Wealth of the Firm	28,20,000	24,20,000	17,60,000

VALUATION OF LIFE INTEREST

Illustration 13. Satender is aged 35 years. His father settled a property in trust giving whole life interest therein to Satender. The income from the property for the years 2007-08 to 2010-11 was ₹ 70,000, ₹ 84,000, ₹ 90,000, ₹ 108,000, respectively. The expenses incurred each year were ₹ 2,000, ₹ 4,000, ₹ 5,000 and ₹ 6,000 respectively. Calculate the value of life interest of Mr. Jogi in the property so settled on the valuation date 31.3.2012, with the help of the factor of 9.267.

Step	Procedure
1	Average Income for last three years = $(₹ 84,000 + ₹ 90,000 + ₹ 1,08,000) / 3 = ₹ 94,000$.
2	Average Expenses for the last three years = $(₹ 4,000 + ₹ 5,000 + ₹ 6,000) / 3 = ₹ 5,000$.
3	Maximum Permissible Expenses = Average Expenses or 5% of Average Income, whichever is less = 5% of ₹ 70,000 = ₹ 3,500
4	Average Annual Income = ₹ 94,000 Less ₹ 3,500 = ₹ 90,500.
5	Life Interest = Average Annual Income × Life Interest Factor = ₹ 90,500 × 9.267 = ₹ 8,38,664.

Illustration 14. 'X' received a vacant site under his father's will. The value of the site on 31.3.2012 is ₹15 Lakhs. As per terms of the 'Will' in the event 'X' wants to sell the site he should offer it to his brother for sale at ₹10 Lakhs. 'X', therefore, claims that the value of the site should be taken at ₹10 Lakhs as at 31.3.2012. Is the claim correct?

Solution :

- As per Rule 21 of Schedule III to the Act, the **price or other consideration for which** any property may be **acquired by or transferred to any person under the terms of a deed of trust** or through or under any restrictive agreement in any instrument of transfer **shall be ignored** for the purpose of determining the value under the provisions of the Schedule.
- In view of the above, the value of the site should be taken as ₹ 15 Lakhs and not as ₹ 10 Lakhs.
- Therefore, **claim of X is incorrect.**

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