



M.Com. PART - II
DIRECT AND INDIRECT TAX

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I

Revised Syllabus of Master of Commerce (M.Com) Programme (To be implemented from the Academic Year - 2018-19 in IDOL)

SECTION I Direct Tax

Modules at a Glance

Sr. No.	Modules
1	Definitions and Basis of Charge
2	Heads of Income
3	Deductions u/s 80 and Exclusions from the Total Income
4	Computation of Income and Tax of Individual, Firm and Company (Excluding MAT) and Provisions for Filing Return of Income - Sec 139(1) and Sec 139(5)

1. Definitions and Basis of Charge

- Definitions: Person, Assessee, Income
- Basis of Charge: Previous Year, Assessment Year, Residential Status, Scope of Total Income, Deemed Income

2. Heads of Income

- Income from Salary
- Income from House Property
- Profits and Gains from Business and Profession
- Income from Capital Gains
- Income from Other Sources

3. Deductions u/s 80 and Exclusions from the Total Income

- Deductions: 80C, 80CCF, 80D, 80DD, 80DDB, 80E, 80U
- Exclusions: Exemptions related to Specific Heads of Income to be Covered with Relevant Provisions, Agricultural Income, Sums Received from HUF by a Member, Share of Profit from Firm, Income from Minor Child, Dividend

4. Computation of Income and Tax of Individual, Firm and Company (Excluding MAT) and Provisions for Filing Return of Income - Sec 139(1) and Sec 139(5)

- Computation of Income & Tax of Individual and Partnership Firm

II

SECTION II

Indirect Tax- Introduction of Goods and Service Tax

Modules at a Glance

Sr. No.	Modules
5	Overview of Goods and Service Tax
6	Registration under GST
7	Collection of Tax under Integrated Goods and Services Tax Act, 2017
8	Place of supply of goods or services or both under Integrated Goods and Services Tax Act, 2017
9	Payment of GST

5. Overview of Goods and Service Tax

- Introduction and Meaning of GST and IGST
- Scope of GST
- Present/old Tax Structure v/s GST
- GST in Other Countries
- Existing taxes proposed to be subsumed under GST
- Principles adopted for subsuming the taxes
- Dual GST
- Benefits of GST
- GST Council
- GST Network (GSTN) and GST regime
- Integrated Goods and Services Tax Act, 2017: title and definitions, administration.

6. Registration under GST

- Rules and Procedure of registration
- Special provisions relating to casual taxable person and non-resident taxable person
- Amendment of registration
- Cancellation of registration
- Revocation of cancellation of registration

7. Collection of Tax under Integrated Goods and Services Tax Act, 2017

- Sec 5 and Sec 6

III

8. Place of supply of goods or services or both under Integrated Goods and Services Tax Act, 2017

- Sec 10 and Sec 12

9. Payment of GST

- Introduction
- Time of GST Payment
- How to make payment
- Challan Generation & CPIN
- TDS & TCS

Note:

- 1. The Syllabus is restricted to study of particular sections, specifically mentioned rules and notifications only*
- 2. All modules/units include computational problems/ Case study*
- 3 The Law in force on 1st April immediately preceding the commencement of Academic year will be applicable for ensuing Examinations.*
- 4. Relevant Law/Statute/Rules in force and relevant Standards in force on 1st April immediately preceding commencement of Academic Year are applicable for ensuring examination after relevant year.*



SECTION- I: DIRECT TAXES

INCOME TAX

1

INTRODUCTION AND BASIC CONCEPTS

Synopsis

1. Introduction and Objectives
2. Assessment Year
3. Previous Year
4. Person
5. Assessee
6. Assessment
7. Income
8. Gross Total Income
9. Total Income
10. Scheme of charging income tax
11. Self Examination Questions

1. INTRODUCTION AND OBJECTIVES :

Under Entry 82 of the Schedule VII to the Constitution of India, the Central Government is empowered to levy 'Tax on income other than agricultural income in India. Accordingly , the parliament has enacted Income Tax Act, 1961["The Act"] to provide for the scope and machinery for levy and collection of Income Tax in India, supported by Income Tax Rules,1962 and several other subordinate rules and regulations.

Further, the Central Board of Direct Taxes (CBDT) and the Ministry of Finance, Government of India issue from time to time circulars and notifications dealing with various aspects of the levy of Income tax.

Unless otherwise stated, references to the sections will be the reference to the sections of the Income Tax Act, 1961.

Section 4, which is the charging section, states that income tax is a **tax** on **the total income** of a **person** called the assessee of **the previous year** relevant to the **assessment year** at the rates prescribed in the relevant Finance Act

This phrase sets the tone and agenda of any study on income tax law. This comprises of the understanding of the following:

- Concept of assessment year and previous year,
- Meaning of person and assessee,
- How to charge tax on income,
- What is regarded as income under the Income-tax Act,
- What is gross total income,
- What is total income or taxable income and
- Income-tax rates

This lesson deals with all these aspects, which lay down the basic framework for levy of income tax in India and explain the basic concepts and terms used in the income tax law.

2. ASSESSMENT YEAR – S. 2(9)

Section 2(9) defines an “Assessment year” as **“the period of twelve months starting from the first day of April every year”**

An assessment year begins on 1st April every year and ends on 31st March of the next year. Hence, the assessment year 2018-19 means the period of one year beginning on 1st April, 2018 and ending on 31st March, 2019.

Income of an assessee during the previous year is taxed in the relevant assessment year. It is therefore, also called as the “tax year”

3. PREVIOUS YEAR- S. 2(34)& S. 3

3.1. Defintion:

Section 3 defines “previous year” as **“the financial year immediately preceding the assessment year”**.

Income earned by an assessee in one financial year is taxed in the next financial year. The year in which income is earned is called the “previous year” and the year in which it is taxed is called the “assessment year”.

This will be explained from the following illustrations:

Illustrations-1:

Income earned during financial year 2017-18 will be taxed in the financial year 2018-19. Hence, 2018-19 will be the assessment year and the preceding financial year 2017-18 will be the previous year.

Illustration -2

For the assessment year 2017-18, previous year will be 2016-17 i.e. from 1st April, 2016 to 31st March 2017.

3.2. Common previous year for all source of income:

A person will be liable to pay taxes on his total income earned from different sources during the previous year. In other words, the previous year will be common for all sources of income, even if he maintains records or books of accounts separately for different sources of income.

Illustration-3:

During the financial year 2017-18, Ashok gets salaries of Rs 10,00,000 from A Limited and Rs 2,00,000 from B Limited. He also earns Rs 2,00,000 from his profession and Rs 3,00,000 as interest on bank fixed deposits. Ashok will be liable to pay tax on aggregate income of Rs 17,00,000 from all the sources i.e. (Rs 10,00,000+ 2,00,000+ 2,00,000 + 3,00,000) earned during the previous year 2017-18 and it will be taxed in the assessment year 2018-19.

3.3. New Business or Profession:

Where a business is newly set up during a financial year or where a new source of income has arisen during that financial year, the previous year will be the period (obviously less than one year) commencing from the date of setting up of the new business or the date of new source of income arising.

Illustration-4

Ramesh sets up a business in January, 2018. The period of three months beginning on 1st January, 2018 and ending on 31st March, 2018 will be the previous year 2017-18 and taxed in the assessment year 2018-19. It is immaterial that previous year is of a period of less than 12 months.

3.4. Exception:

Ordinarily the income of the previous year is taxable in the next assessment year. However, in some cases an assessee is liable to pay tax on the income in the same previous in which he earns it. These exceptional cases ensure safeguards to smooth collection of income tax from a class of taxpayers who may not be traceable until the commencement of the normal assessment year. In such cases, previous year and assessment year will be the same. Some of such exceptions are as under:-

- a) Realisation of bad debts written off in the earlier years and allowed as deduction – Sec. 41(1)
- b) Deemed dividend – Sec. 56

- c) Income of non-residents from shipping business–Sec.172;
- d) Income of persons leaving India permanently or for a long period of time and not likely to return back –Sec. 173-174;
- e) Income of bodies formed for short duration for a particular event or purpose – Sec 174A;
- f) Income of a person trying to alienate his assets with a view to avoiding payment of tax – Sec. 175 ,
- g) Income of a discontinued business- Sec.176

4. . PERSON –S. 2(31)

4.1 Definition:

Section 2(31) gives an inclusive definition of “person”

“Person” includes:

- a) an individual;
- b) a Hindu undivided family (HUF);
- c) a company;
- d) a firm;
- e) an association of persons(AOP) or a body of individuals,(BOI) whether incorporated or not;
- f) a local authority; and
- g) every artificial juridical person not falling within any of the preceding categories

4.2 Inclusive definition:

Since the above definition of “person” is inclusive one and not exhaustive, there may be cases, when an entity not falling in the above seven categories may still be treated as “person” inviting the provisions of the Act.

4.3 Profit motive not necessary:

As per Explanation to Sec. 2 (31), an entity need not be formed for profit. Non-Profit Organisations or charitable trusts are also covered by the definition of “person” although their income is not taxable under the Act on satisfying the certain terms and conditions.

4.4 Description of types of persons :

A brief description of these seven categories is as follows:

- a. **Individuals** are all living persons of blood and flesh e.g. Ram, Shyam, Gopal, Albert, Ibrahim etc.

- b. **Hindu Undivided Families (HUF)** or Hindu joint families are regarded as separate tax entities in view of the specific law of succession prevalent among the Hindus.
- c. **Company** as per section 2(31) includes any Indian, foreign, public or private Company. Even Companies incorporated u/s 8 of the Companies Act, 2013 (corresponding to section 25 of the Companies Act, 1956) for charitable purpose are also covered by the definition of company, although they can claim exemption from tax on compliance of the legal conditions given in other provisions of the Act. Further, the CBDT has the power to declare any institution as a company.
- d. **Partnership firms** including limited liability partnerships (LLPs) are regarded as distinct taxable units separate from their partners. Therefore, under the Act, firms are taxed as the firms and individual partners are taxed separately in their personal capacity.
- e. Body of individual (**BOI**) and association of persons (**AOP**) are the group of persons carrying on some activities to earn income such as joint venture.

Normally, AOPs are contractual in nature like a joint venture agreement if such venture not formed as a partnership or a company.

On the other hand, BOI may be due to circumstances such as joint owner of a estate. clubs, societies, charitable trusts etc. are covered under this head.
- f. Municipal corporations, panchayats, cantonment boards, zila parishads etc. are the examples of Local authorities.
- g. Final category is residual category and covers all such persons which are not covered in any of the above six categories.

Illustration-5:

Determine the status in the following persons as per the Income Tax Act, 1961:

Person	Status
Ramesh Agrawal	Individual
Asha Jain	Individual
Reliance Industries limited	Company
Warna Co-Society Ltd	AOP
Indian Red Cross society	AOP

Legal heirs to receive property of late Shri Nusserwanji	BOI
Tata power Ltd	Company
Sachin Tendulkar	Individual
Board for Cricket control in India	AOP
Family of Shri PB Hindu	HUF
Pune Cantonment Board	Local Authority
Mumbai University	Artificial Juridical Person
Ramsay Brothers doing business in partnership	Firm

5. ASSESSEE–S. 2(7)

5.1 Definition :

U/s 2(7) “assessee” means a person by whom income tax or any other sum of money is payable under the Act and it includes:

- a. every person in respect of whom any proceeding under the Act has been taken for the assessment of his income or assessment of fringe benefits or of the income of any other person in respect of which he is assessable, or of the loss sustained by him or by such other person, or of the amount of refund due to him or to such other person ;
- b. every person who is deemed to be an assessee under any provision of this Act ;
- c. every person who is deemed to be an assessee in default under any provision of this Act.

5.2 The definition of “assessee” is also inclusive and very broad in scope. It includes any other person not covered in the above categories. The definition covers not only a person but also his representative such as legal heir, trustee, liquidator of a company assessee etc. Moreover, importance is given to not only the amount of tax payable but also to refund due and the proceedings taken.

5.3 Thus, an assessee may be :-

1. A person by whom income tax or any other sum of money is payable under the Act
2. A person in respect of whom any proceeding under the Act has been taken for the assessment of his :
 - a. income or
 - b. loss or
 - c. the amount of refund due to him

3. A person who is assessable in respect of income or loss of another person or
4. A person who is deemed to be an assessee,
5. an assessee in default under any provision of the Act

5.4 A minor child is a separate assessee, but his income is included in the income of the parent having the higher income unless, such income is from an asset assets acquired from the minor's sources of income or income generated out of activities performed by him like singing in radio jingles, acting in films, tuition income, delivering newspapers, etc.

6. ASSESSMENT - S 2(8)

In an inclusive definition, section 2(8) states “**an assessment includes reassessment**”.

Assessment is the procedure to determine the taxable income of an assessee and the tax payable by him.

U/s 139 of the Act, every assessee is required to file a self-declaration of his income and tax payable by him called “return of income”.

The Income Tax officer may accept the return summarily without making any enquiry into its contents. This is called as the ‘summary assessment’ under section 143(1).

Alternatively, the officer calls upon the assessee to explain his return of income and after making necessary enquiry , frames a reasoned order determining the total income and the tax payable by the assessee this is called the “regular assessment” under section 143(3).

Completed assessment becomes final except in certain circumstances. These circumstances are:

- a. U/s 147, an assessment can be reopened to assess income which has escaped assessment,
- b. U/s 263 , the Commissioner of Income Tax may ask an assessment to be redone if the assessment order is erroneous and prejudicial to the interest of the revenue ,
- c. U/s 264, the Commissioner of Income Tax at the application of an assessee or *suo motu*, may ask an assessment to be redone. This is normally done to give relief to the assessee.

- d. U/s 254, the Income Tax Appellate Tribunal (ITAT) in appeal proceedings may pass an order directing the assessment to be redone.

In all the above cases, "reassessment" of the income is required to be done. The definition of assessment includes the regular assessment and reopened or reassessment.

7. INCOME- S 2(24)

7.1 Definition :

Sec 2(24) gives an inclusive definition of income. It states that Income" includes—

- (i) profits and gains ;
- (ii) dividend;
- (iia) **voluntary contributions** received by
 - a trust created wholly or partly for **charitable for religious** purposes, or
 - any institution , an association or a fund or trust or institution for **scientific research** u/s 10(21) / (23);
 - any university or other **educational institution** referred to in section 10 (23)(iiia) or(vi) (**sports body**) ;
 - any **hospital** or other institution u/s 10(23C) (iiiae) or (via),
 - by an **electoral trust**.

For this purpose, "trust" includes any other legal obligation ;

Receipt by employees

- (iii) the value of **any perquisite or profit in lieu of salary** taxable under section 17(2) / (3) ;

(iiia) **any special allowance or benefit**, (other than perquisite) , specifically granted to the assessee to meet expenses wholly, necessarily and exclusively for the performance of the duties of an office or employment of profit ;

(iiib) any 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 a place where he ordinarily resides or to compensate him for the increased cost of living(**City Compensatory Allowance**) ;

(iv) the value of any **benefit or perquisite**, whether convertible into money or not, obtained from a company either by a director or by a person who has a substantial interest in the company, or by a relative of the director or such person, and any sum paid by any such company in respect of any obligation which, but for such payment, would have been payable by the director or other person aforesaid ;

(iva) the value of any **benefit or perquisite**, whether convertible into money or not, obtained by any representative assessee mentioned in section 160(1)(iii) or (iv) of or by any person on whose behalf or for whose benefit any income is receivable by the representative assessee (the "beneficiary") and any sum paid by the representative assessee in respect of any obligation which, but for such payment, would have been payable by the beneficiary ;

(v) any sum chargeable to income-tax((**Balancing charge**) under section 28(ii) / (iii) or section 41 or section 59) ;

Benefits to exporters

(va) Duty drawback under section 28 (iiia) ;

(vb) Cash Assistance under section 28 (iiib) ;

(vc) DEPB under section 28 iiic) ;

(vd) the value of any benefit or perquisite taxable u/s 28 (iv) ;

(ve) any sum chargeable to income-tax u/s 28 (v) ;

(vi) any **capital gains** chargeable under section 45 ;

(vii) the profits and gains of any **business of insurance** carried on by a mutual insurance company or by a co-operative society, computed in accordance with section 44 or any surplus taken to be such profits and gains by virtue of provisions contained in the First Schedule ;

(viiia) the profits and gains of any **business of banking** (including providing credit facilities) carried on by a co-operative society with its members;

(viii) Omitted

(ix) any winnings from **lotteries, crossword puzzles, races** including horse races, card games and other games of any sort or from gambling or betting of any form or nature whatsoever.

For this purpose,—

(i) "lottery" includes winnings from prizes awarded to any person by draw of lots or by chance or in any other manner whatsoever, under any scheme or arrangement by whatever name called;

(ii) "card game and other game of any sort" includes any game show, an entertainment programme on television or electronic mode, in which people compete to win prizes or any other similar game ;

(x) 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 ;

(xi) any sum received under a Keyman insurance policy including the sum allocated by way of bonus on such policy.

(xii) any sum referred to in section 28 (va) ;

Gifts without consideration

(xiii) any sum referred to in section 56 (2)(v);

(xiv) any sum referred to in section 56 (2)(vi);

(xv) any sum of money or value of property referred to in section 56 (2) (vii) a) ;

(xvi) any consideration received for issue of shares as exceeds the fair market value of the shares referred to section 56(2) (vii) b)

(xvii) any sum of money referred to in section 56 (2)(ix);

(xviii) any sum of money or value of property referred to in section 56 (2)(x)

(xviii) assistance by way a **subsidy or grant or cash incentive** or duty drawback or waiver or concession or reimbursement (by whatever name called) by the Central Government or a State Government or any authority or body or agency in cash or kind to the assessee other than,—

(a) the subsidy or grant or reimbursement which is reduced from the actual cost of the asset u/s 43 (1) Explanation 10;or

(b) the subsidy or grant by the Central Government for the purpose of the corpus of a trust or institution established by the Central Government or a State Government,

7.2. Sec 2(24) gives an inclusive definition of income. As per the section, “income” covers not only the income in its natural and general sense but also several items not otherwise considered as income.

Hence, Income means not only the revenue receipts arising or accruing regularly but also capital receipts like gifts and even donations and gifts. On the other hand, certain revenue receipts like agricultural income are left out from the scope of the term income.

Some of the principles that have emerged out as a result of customs, practices and judicial pronouncements to ascertain as to what does or does not constitute income are as follows.

1. Ordinarily Income is a regular periodical receipt, received or derived from a certain source.
2. The source of income must be external. No one can earn income by or from himself.
3. On this principle, income accruing to clubs, societies etc. from their own members are not taken as taxable income on the ground of mutuality.
4. Normally, only revenue receipts are regarded as income unless specifically exempted.
5. On the other hand, capital receipts are not treated as income unless the law specifically provides e.g. capital gains, gifts, maturity proceeds of keyman insurance policy, sales tax subsidy, voluntary contribution by a donor to a trust , which are included in income in spite of being capital receipts .

Income is like the fruit of a tree, where tree is the source, or the capital asset.

6. Income may be in cash or kind.
7. Income need not be legal. It may even be derived from illegal sources like, smuggling, theft, bribery, corruption etc.
8. It is the receipt, which is income not its application or use.
9. Any receipt diverted at the origin or the source by overriding title will not be regarded as income.
10. Any dispute in the title of the income does not take away its nature as income.
11. A gift is a capital receipt given for personal considerations. However, the is no longer valid proposition as the law specifically provides for taxation of gifts, e.g.:-
 - gift by an employer to an employee is deemed to be taxable salary u/s 17.

- Gift by a client or customer is deemed as the income under the head profits and gains from business or profession u/s 28. Hence, a gift given by a client to his lawyer or chartered accountant or a patient to his doctor, or a disciple or pupil to his guru, will be taxable as the income of the recipient (donee) from business or profession u/s 28 .
 - Personal gifts in excess of Rs. 50,000, from all sources are taxable as income from other sources u/s 56 subject to certain exceptions. Further. Inadequate consideration on transfer of immovable or movable assets is also considered as taxable gift u/s 56. This aspect is dealt with in great detail in the lesson relating to income from other sources
12. Income may be recognised either on receipt basis or on accrual basis depending upon the facts and circumstances of and the method of accounting applied in each case.
 13. Income must be certain. Contingent income is not regarded as income unless and until such contingency occurs and the income arises to the assessee.
 14. Income is the sum total of all receipts from all the sources and considered accordingly.
 15. Pin money received by a woman for personal expenses or even the savings made by her from such receipts is not considered as income. However, the husband will not get any credit from his income for these payments.
 16. Income may be received in lump sum or in instalments. Thus, arrears of salary received by a person in lump sum are regarded as his income.
 17. Awards received by a professional sportsperson would be income, unless the award is in nature of a gift for personal consideration.
 18. Income of wife is be taxable in the hands of the husband, if the assets out of which the income is arising have not been acquired out of the sources of the wife or from an asset gifted by the husband except as consideration for living apart.
 19. Income of minor children is be taxable in the hands of the parents having higher income [mother or father] except when the income is arising from the efforts of the minor child say modeling charges.

8. GROSS TOTAL INCOME- S -14:

Section 14 of the Act defines the gross total income as the aggregate of the incomes computed under the five heads after adjusting for set-off and carry forward of losses. The five heads of income are as follows namely:

1. Income from Salaries
2. Income from House Property
3. Profits and Gains from Business & Profession
4. Capital Gains
5. Income from Other Sources

The gross total income is the aggregate of income computed in accordance with the provisions of the Act under the five heads, before making any deduction under sections 80C to 80U. It may be noted that, any income exempted from tax u/s 10 or other provisions conveyance allowance, capital gains on sale of personal effects, dividend income, etc.; is not considered or excluded from the income computed under the respective heads.

9. TOTAL INCOME:

The total income of an assessee is computed by deducting from the gross total income all permissible deductions available under the Chapter VI A of the Income Tax Act, 1961. This is also referred to as the “Net Income” or “Taxable Income”.

10. SCHEME OF CHARGING INCOME TAX

Income tax is a tax on the total income of an assessee for a particular assessment year. This implies that;

- ♦ Income-tax is an annual tax on income
- ♦ Income of previous year is chargeable to tax in the next following assessment year at the tax rates applicable for the assessment. year This rule is, however, subject to some exceptions discussed above.
- ♦ Tax rates are fixed by the annual Finance Act and not by the Income-tax Act. For instance, the Finance Act, 2018 fixes tax rates for the financial year 2017-18 relevant to assessment year 2018-19. Tax rates are given in the lesson dealing with computation of income.
- ♦ Tax is charged on every person if the total income exceeds the minimum income chargeable to tax.

11. SELF ASSESSMENT QUESTIONS

1. Income of a previous year is chargeable tax in the immediately following assessment year. Is there any exception to this rule? Discuss

2. Define the term “person”
3. How would you calculate income tax for the assessment year 2018-19 in the case of different assesses?
4. Explain how education cess will be computed for the assessment year 2018-19? [Ans: 2%+1%]
5. What will be the previous year for X, who starts his business on April 6, 2014[Ans: A.Y. 2015-16]
6. Will the answer to Q 5 be different, if X starts his business on 28th March, 2014? [Ans: A.Y. 2014-15]
7. Explain that a financial year is a previous year and also an assessment year. Every financial year can also be an assessment year,
8. Previous year is a financial year immediately preceding the Assessment year Comment
9. What will be the status of University of Mumbai?
[Ans: Artificial juridical person]
10. Indicate whether the following persons will be taxed as individuals:
 - a) X a partner of a firm
 - b) Y, a managing director of A Ltd;”
 - c) Z is the member of Z HUF
 - d) Municipal Commissioner of Mumbai in respect of the Income of the Municipal Corporation
 - e) Municipal Commissioner of Mumbai in respect of his salary from the Municipal Corporation
 - f) A minor acting in TV commercials

[Ans: All except (d) will be taxed, Firm X, A Ltd, Z HUF, Mun Corpn. Separate tax entities]



BASIS OF CHARGE AND INCIDENCE OF TAX

Synopsis

1. Introduction and Objectives
2. Basic Charge of Income Tax
3. Residential Status
4. Residential status and incidence of tax
5. Income deemed to be received in India
6. Income deemed to accrue or arise in India
7. Receipt vs. Remittance
8. Actual receipt Vs. Deemed Receipt Total Income
9. Receipt vs. Accrual
10. Basis of Charge of Dividend Income
11. Heads of Income
12. Self-Examination Questions

1. INTRODUCTION AND OBJECTIVES

This lesson deals with the scheme of income Tax laid down in section 4 to 9 as to the basis of charging income tax , income on which tax is to be levied , the status of persons and effect of the status of persons on which the income tax is to be levied, periodicity of the tax and other incidental matters .

2. BASIS OF CHARGE OF INCOME TAX (Ss. 4-9)

Section 4 to 9 lay down a detailed scheme and basis of charge of income tax in India

I. Charge of income tax- section 4

Under section 4(1), income tax shall be charged for **any assessment year** at any rate or rates prescribed in the Finance Act in respect of the **total income** of the **previous year** of **every person**

In brief section 4 envisages that :

- Tax is payable(including by way deduction at the source or paid in advance) ;
- on total income ;

- of a person called assessee ;
- during the previous year or a period other than the previous year (as per proviso to the section) ;
- relevant to assessment year ,
- at the rate or rates prescribed in the Finance Act ,

II. Scope of total income- Section 5

Under Section 5 total income of an assessee is chargeable to tax depending upon

- a) the residential status of a person; and
- b) place and time of accrual of such income.

III. Residential statues and place – Section 6

Section 6 provides the rules for determining residential status of different types of persons

IV. Income accrued or received in India –Ss. 7-8 & 9

- Section 7 certain specifies the incomes , which are not received in India but are deemed to be received in India.
- Section 8 deals with the year of taxability of dividend income
- Section 9 specifies the incomes though not accrued or arisen in India but are deemed to accrue or arise in India.

3. RESIDENTIAL STATUS –SECTION- 6

3.1 As per section 5, total income of an assessee is chargeable to tax depending upon the residential status of a person; and place and time of accrual of such income and section 6 prescribes the rules for determining residential status of different categories of persons. These provisions are discussed in detail below.

3.2 Classification of persons:

Provisions for determination of the residential status are different for different categories of the assessee viz:-

- a) individuals;
- b) Hindu Undivided Families (HUF)
- c) Firms, BOI or Associations of Persons(AOP);
- d) Companies; and
- e) Every other person

3.3 Residential status of individual:

3.3.1 Basic conditions: -Section 6(1):

As per section 6(1) , an individual is said to be a resident in India in any previous year, if he satisfies **at least one** of the following **TWO basic conditions viz. : —**

- a) He is in India in that previous year for a period or periods amounting in all to **182 days or more** OR
- b) He has been in India is in India for a period or periods amounting in all to **365** days or more during **4** years immediately preceding that previous year **AND**

He is in India in that previous year for a period or periods amounting in all to **60** days or more during that previous year.

Exception:

The limit for stay in India for **60 days or more** as per condition (b) will be extended to **182 days or more** in following two circumstances:

- i. **An Indian citizen leaves India** during the previous year
 - for the purpose of taking up employment outside India ; OR
 - as a member of the crew of an Indian ship;OR
- ii. **An Indian citizen or a person of Indian origin (PIO) comes on visit** to India during the previous year.

A person is said to be of Indian origin (PIO) if either he or any of his parents or grandparents was born in undivided India.

To sum up, in both the cases, an individual needs to be present in India for a minimum of **182 days or more** to become resident in India **instead of 60 days**. This may result in two possibilities:

- a) An individual may not satisfy either of the two conditions; or
- b) An individual may satisfy any or both of the two basic conditions , then the individual will be -
 - In case(a), **a non- resident; and**
 - in case (b), **a resident of India**
 for that particular assessment year.

3.3.2 Resident and Ordinarily Resident [R & O R]-Sec-6(6)

If a person is a resident of India) in a particular previous year, as per section 6(1), next step would be to determine whether he will be a resident and ordinarily resident of India in that previous year as per Section 6(6).

Section 6(6) provides that a person will be “**resident and ordinarily resident**” in India in any assessment year if he satisfies **BOTH** of the following two conditions that he has been-

- 1) resident in India in 2 out of 10 previous years immediately preceding that previous year as per S. 6(1) ; AND
- 2) in India for a period of, or periods amounting in all to, 730 days or more during the seven previous years preceding that previous.

In simple words,

- a) an individual must be resident in India in at least 2 years out of 10 years immediately preceding that previous year as per AND
- b) he must be in India for a period of 730 days or more .

3.3.3 Resident and Not Ordinarily Resident [R &N O R]

A resident individual, who does not satisfy BOTH of the above conditions given above, will be a Resident but Not Ordinarily Resident in India. Hence, an individual becomes resident but not ordinarily resident in India If he -

- (a) is non-resident in 9 out of 10 previous years immediately preceding that previous year or
- (b) has during the seven previous years preceding that year been in India for a period of, or periods amounting in all to, 729 days or less.

It is not enough that an Individual satisfies only one of the additional conditions. Such individual Resident and Not Ordinarily Resident (R &N. O. R.)

In other words, R &N. O. R is an individual, who-

- satisfies at least one of the basic conditions but satisfies NONE of the additional conditions ,or
- Satisfies ONLY ONE of the two additional conditions.

3.3.4 Non- Resident

An individual is a non-resident in India if he satisfies none of the basic conditions. It must be noted that if a person satisfies the additional conditions but does not satisfy the basic conditions, he will still be treated as Non-Resident. In such a case, additional conditions are not relevant.

3.3.5 SUMMARY

To sum up , an individual can either be:

- (a) resident and ordinarily resident in India;
- (b) resident but not ordinarily resident in India; or
- (c) non-resident

Following table gives the summary of the provisions

Status of the Individual	Basic Conditions Section 6(1)	Additional Conditions – Section 6(6)
Resident and ordinarily Resident	Must satisfy either of the two conditions	Must satisfy BOTH conditions
Resident but not ordinarily Resident	Must satisfy either of the two conditions	MUST NOT satisfy any one or both the conditions
Non Resident	Does not satisfy any conditions	Not necessary that the two conditions are satisfied or not.

3.3.6 Some Important points:

Following points are important in determining the residential status of a person :

- a) In computing the day on which a person is in India
 - i. Stay may be at one place or more than one place. Stay at different places in India will be aggregated.
 - ii. Stay in India may be continuous or in intervals. Stay in intervals will be aggregated.

Both the day of arrival in India and departure from India shall be considered even if on such days the person is in India only for a part of a day. However, the courts have held that *a total of 24 hours of stay spread over a number of days is to be counted as being equivalent to the stay of one day. Students are advised to consider the day of departure and arrival both as two days, if the hours of arrival and departure are not given.*
- b) *A person, who is in India for 182 days or more, will always be a resident of India.*
- c) *Conversely, a person, who is in India for 59 days or less, will always be Non-Resident of India.*
- d) An Indian citizen must leave India **for employment or as crew to** avail extended limit of 182 days instead of 60 days
- e) An Indian citizen leaving India Resident and ordinarily in India will not get the extended time limit of 182 days.
- f) The condition is relaxed only for Indian citizens and not for persons, who are not Indian citizens.
- g) Indian citizens or persons of Indian origin(PIO) must come to India **on visit** for any purpose – pilgrimage, medical treatment or tourism but NOT business or job to avail

extended limit of 182 days Indian citizenship is not the requirement for this purpose.

- h) While computing the period of stay, note that 2008, 2012 and 2016 were leap years with one extra day.

3.3.7 Illustrations :

Illustration -1:

Rajesh leaves India for the first time on December 20, 2010. During the financial year 2017-18, he came to India on May 27 for a period of 45 days. Determine his residential status for the assessment year 2018-19

Solution:

During the previous year 2017-18, Rajesh is in India only for 45 days He does not satisfy any of the basic conditions laid down in section 6(1). Hence, Rajesh is a non-resident in India for the assessment year 2018-19

Illustration -2:

Mahesh comes to India, for the first time, on April 16, 2015. He stays in Chennai up to April 29, 2017 and thereafter shifts to Mumbai. He departs from Mumbai for his native country on October 8, 2017. Determine his residential status for the assessment year 2018-19

.Solution:

- During the previous year 2017-18 , Mahesh is in India for (April 30+May 31+ June+30+ July 31+ August 31+ Sept 30 +Oct. 5)= 188 days, he is a resident in India u/s 6(1) as he is in India for more than 182 days
- During the previous year 2015-16, Mahesh was in India for 351 days from 16/04/2015 to 31/03/2016 (leap year) and for the full year or 365 days in 2016-17. Mahesh is resident in India for these two years. He fulfills the first additional condition under Section 6(6) that he must be a resident in India in at least two year out of the ten preceding years.
- Mahesh was in India for a period of 716 days only [351 days in 2015-16 and 365 days in 2016-17 ,which is less than 730 days stay required in the seven preceding years. Hence, Mahesh does not satisfy the second condition as per Sec 6 (6)
- Mahesh satisfies one of the basic conditions and only one of the two additional conditions, he is, therefore, resident but not ordinarily resident in India for the A.Y. 2018-19

Illustration -3:

Determine residential status for the assessment year 2018-19, of Venkat, an Indian Citizen who leaves India for employment in Canada on July 1, 2017.

Solution:

Venkat was in India for 92 days in 2015-16 (April : 30 days; May - 31 days; June : 30 days and July 2011: 1 day). Venkat is an Indian citizen, leaving India to take up a job. Hence he will be get the extended limit of 182 days' stay in India during 2016-17. Hence Venkat will be a non -resident although he was in India for more than 365 days during the four years preceding the previous year

Illustration - 4:

What will be the position in the above case, if Venkat leaves India for world tour?

Solution:

Venkat will be Resident and Ordinarily Resident of India as he satisfies the second basic condition u/s 6(1) of 365 days' stay in the preceding four years and 60 days' stay during 2016-17 and also the two additional condition of section 6(6), as being a person born in India, Venkat satisfies both the additional conditions of being resident in India for two years in preceding 10 years and stay of 730years in seven preceding years.

Illustration -5:

Supposing in the above case, Venkat wants to postpone his stay in India, what would be the last date by which he should leave India?

Solution:

Venkat is covered by the exception, he should depart latest by September 28, 2017 so that his stay in India during the previous year 2016-17 is of 181 days (less than 182 days).

Illustration -6:

What will be the position in the above case, if Venkat is a Nepali citizen settled in India?

Solution

Venkat will not be covered by the exception u/s 6(1) as he is not an Indian citizen. Since he satisfies the basic condition and also both the additional conditions of 730 days in 7 preceding years and 2 years resident in preceding 10 years, he will be a resident and ordinary resident in India

Illustration -7:

Chappell, an Australian Citizen comes to India as the Coach of Indian Cricket team. During the previous year 2016-17, he stays India for 95 days. Before that, he was in India for more than 365 days during the 4 years prior to 2016-17. What will be his residential status for the assessment year 2018-19?

Solution:

Chappell satisfies the second basic condition of stay of 365 days or more during the four years preceding the previous year 2016-17, and he was in India for more than 60 days during

the financial year 2016-17. He is Resident of India. Since he is not a person of Indian origin nor he comes in India on visit, he will not get the extended time limit of 182 days. Since Chappell was never in India, he does not fulfill the additional two conditions, hence he will be Resident but not Ordinarily Resident of India [RNOR] .

Illustration -8:

Will the position be different in the illustration 7, if Chappell is a resident of Bangladesh?

Although Bangladesh was part of undivided India, Chappell will not get any benefit as he has not come on visit but as a professional coach.

Illustration -9:

Will the above position change if Chappell is a Pakistani citizen and visits India as a tourist?

Solution:

Yes, Chappell will get the extended limit of 182 days and he will be a Non- resident.

3.4. Residential status of HUF :

3.4.1 Resident

As per Section 6(2), a Hindu Undivided Family (HUF) will be:

- **Resident** in India if control and management of its affairs is **wholly or partly** situated in India.
- **Non- resident** in India, only if control and management of its affairs is situated **wholly outside** India.

3.4.2 Resident and Ordinarily resident (ROR)

U/s 6(6) , a HUF can will be Resident and Ordinarily Resident if its Karta or manager satisfies **both** of the following **two conditions** viz.the Karta or the manager :-

- (a) has been a non-resident in India in 9 out of the 10 previous years preceding that year, and
- (b) has during the 7 previous years preceding that year been in India for a period of, or periods amounting in all to 729 days or less

It may be noted that additional conditions are same as those applicable to the individual but applicable on the Karta or the manager of a HUF.

3.4.3 Resident and Not Ordinarily resident (RNOR)

If the Karta does not satisfy both of the two additional conditions, the HUF will be treated as a **resident but not ordinarily resident** (RNOR) in India

3.4.4 Non-Resident

A HUF will be **non- resident** in India ONLY if control and management of its affairs is situated **wholly outside India**.

It is important that place of control and the management of HUF is relevant to determine whether the HUF is Resident or Non-Resident.

However, to determine ROR status the two additional conditions will be applicable with reference to its Karta or Manager.

3.4.5 Summary

Thus, like an Individual a HUF may be either:-

- (a) Resident and ordinarily in India if is controlled or management wholly or partly in India or
- (b) Non-resident in India if its control or management is wholly outside India.
- (c) Resident and ordinarily in India if two additional conditions are satisfied as per Sec 6(6) by the Karta / Manager.

3.5. Residential Status of Other Non-Company Persons (S. 6(2) / S 6(4))

3.5.1 Resident –S 6(2) :

Under Section 6(2) Residential status of all non-company persons viz a firm an Association of Persons (AOP) or a Body of Individuals (BOI) and every other person will also depend upon the place of control and management like HUFs.

Any such person will be:

- **Resident** in India if control and management of its affairs is **wholly or partly** situated in India, ;
- **non-resident** in India if control and management of its affairs is situated **wholly outside** India.

3.5.2 Non Resident

An AOP, BOI or a firm will be non-resident in India if control and management of its affairs is situated **wholly outside** India.

These persons can only be either resident or not resident but not ordinarily resident.

Illustration -10:

An entity XYZ has its operations in India but it takes instructions from London either wholly or partly.

What will be the residential status of XYZ if it is HUF, c) AOP, d) BOI , e) Artificial juridical person?

Solution

XYZ will be Resident of India in all the cases.

Illustration -11:

What will be the status in the above cases, if XYZ is wholly controlled from Mauritius?

Solution

XYZ will be Non -Resident of India in all the cases.

It is important to note that control and management means *de facto* (actual) control or management but not merely the right to control or manage. Place of control and management is situated where the decision making of the entity as a whole is situated.

3.6. Residential Status of a Company –Section 6(3)

A company will be resident of India in any previous year, if—

- (i) it is an Indian company; or
- (ii) its **place of effective management** (POEM), in that year, is in India.

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

From the above, it follows that :-

- 1 Residential status of a company is based on its place of registration and control and management.
- 2 An Indian company will be resident in India irrespective of where their control or management is.
- 3 Any other company (i.e. a foreign company) will be a Resident in India if place of effective management (POEM) of such company is situated in India.
- 4 A foreign company will be non-resident if their control and management is wholly in India if place of effective management (POEM) of such company is situated outside India.

The legal provisions are summarised in the following table.

Company	Status
Indian company	Resident
Foreign company if POEM is situated in India	Resident
Foreign company if POEM is situated outside India	Non resident

Illustration -12:

What will be the residential status of X LTD an Indian company managed from India?

Solution

X Ltd. being an Indian company will be Resident in India. Place of management is immaterial.

Illustration -13:

What will be the residential status of Y LTD an Indian company managed from London?

Solution

Y Ltd. being an Indian company will be Resident in India. Place of management is immaterial.

Illustration -14:

What will be the residential status of T LTD a British company managed from India?

Solution

T Ltd. will be resident in India as its POEM is situated in India.

Illustration -15:

What will be the residential status of U Inc. a US Company managed from London?

Solution

U limited will be a Non-resident in India as its POEM is wholly situated outside India.

3.7. Miscellaneous:

Following points are noteworthy:

(a) Residential status for each previous year:

Residential status of a person shall be determined for each previous year independently.

(b) Different residential status for different assessment years:

Residential status may change from previous year to previous year and a person may have different residential status for different assessment years. For instance, if a person leaves India for two years and then comes back, he can be non-resident for those two years and resident for other years.

(c) Resident in India and abroad:

A person may be “resident” in two or more countries in a particular year. Similarly, in a particular assessment year, a person may be a non-resident in India as well as other countries.

In other words, It is not necessary that a person, who is “resident” in India, will necessarily be non-resident in all the other countries for the same assessment year.

This is particularly true of a person, who has changed his country two three times in a year and he does not fall in any category of residents anywhere in the world.

(d) Residence for all sources:

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)]

4. RESIDENTIAL STATUS AND INCIDENCE OF TAX

Section 5 defines the scope of total income taxable in India. Brief provisions of the section are given as under :-

4.1. Scope of total income for a Resident

As per Sec 5(1) the total income of any previous year of a person who is **a resident** includes all income from whatever source derived which —

- (a) is received or is deemed to be received in India in such year by or on behalf of such person ; or
- (b) accrues or arises or is deemed to accrue or arise to him in India during such year ; or
- (c) accrues or arises to him outside India during such year .

4.2. Person not ordinarily resident in India

The section provides that total income of a person who is not ordinarily resident in India within the meaning of Sec 6(6) shall not include the income which accrues or arises to him outside India unless it is derived from a business controlled in or a profession set up in India. Thus the Income of such person shall include the following income from whatever source derived which—

- (a) is received or is deemed to be received in India in such year by or on behalf of such person ; or
- (b) accrues or arises or is deemed to accrue or arise to him in India during such year ; or
- (c) accrues or arises to him outside India during such year if such income is derived from a business controlled in or a profession set up in India

4.3. person who is a non-resident

As per Sec 5(2) the total income of any previous year of a person who is a non-resident includes all income from whatever source derived which—

- (a) is received or is deemed to be received in India in such year by or on behalf of such person ; or
- (b) accrues or arises or is deemed to accrue or arise to him in India during such year.

Thus the total income of a non-resident shall not include accrues or arises to him outside India during such year.

4.4. Important points

Following are some important points with regard to the scope of total income as per the provisions of Sec 5

- (a) Incidence of tax on a taxpayer depends on:-
 - his residential status, and
 - the place and time of accrual or receipt of income.;
- (b) Income accruing or arising outside India shall not be deemed to be received in India by reason only of the fact that it is considered in a balance sheet prepared in India.
- (c) income which has been included in the total income of a person on the basis that it has accrued or arisen or is deemed to have accrued or arisen to him shall not again be so included on the basis that it is received or deemed to be received by him in India.
- (d) **Indian income will be taxable in all cases.** Indian income or Income received, accruing or arisen in India or deemed to be received, accruing or arising in India will be included in the income of every person regardless of his residential status whether resident , non-resident, or R & OR or R & NOR.

Income may be **Indian income** in a previous year if :-

- Income is received or deemed to be received in India and such income is also accrued or arisen or deemed to be accrued or arisen in India;
 - If income is received or deemed to be received in India BUT it **accrues or arises outside India; or**.
 - If income **is received outside India** but it accrues, arises, or is deemed to accrue or arise in India.
- (e) **“Foreign income”** or income which is not Indian Income or Income not received, accrued or arisen in India nor deemed to be received, accrued or arisen in India is taxable as under:-
- I. Foreign income is not included in the total income of a non-resident,
 - II. Foreign Income is included in the total income of a resident and ordinarily resident ,

- III. Foreign income **will not be** included in the total income of a resident but not ordinarily resident RNOR unless such income is derived from:

- a business controlled in India or
- A profession set up in India

Non-business foreign income will not be included in the income of a person who is resident but not ordinarily resident in India.

Thus foreign income taxable only by a ROR and conditionally by RNOR

- (f) Residents will be liable in respect of all income Indian or foreign but Non- residents liable for Indian income only

The Scope of total income chargeable to tax is summarised as follows:

Scope of total income –S 5			
Income	Status		
	Resident & Ordinarily Resident	Resident & Not Ordinarily Resident	Non Resident
Indian income	Taxable	Taxable	Taxable
Foreign income	Taxable	Taxable if income is from <ul style="list-style-type: none"> • a business controlled from India or • a profession set up in India 	Not Taxable

4. INCOME DEEMED TO BE RECEIVED IN INDIA- SECTION 7

As per section 7, the following incomes are included in the scope of total income even if they are not actually received in India:

1. Annual accretion to the credit balance of an employee in the case of recognized provident fund to the extent provided under rules
2. Excess contribution of employer in the case of recognized provident fund to the extent as provided in the rules.
3. Transfer balance to a recognized provident fund from unrecognized provident fund to the extent as provided under the rules.

5. INCOME DEEMED TO ACCRUE OR ARISE IN INDIA- SEC 9

As per Section 9, which is a deeming section, certain incomes are deemed to accrue or arise in India even though they may actually accrue or arise outside India. These incomes are given below:

1. All incomes accruing or arising whether directly or indirectly through or from-
 - a. Any business connection in India or
 - b. Any property in India or
 - c. Any asset or any source of income in India or
 - d. The transfer of a capital asset situated in India.

Exceptions: No income is deemed to accrue or arise in following cases:

- I. **Purchase of goods** India by a Non- resident for Export,
- II. **Collection of news** by a non- resident running a new agency, or publishing newspapers, magazines or journals,
- III. **Shooting of film** in India by a non-resident foreign citizen individual or a company or firm in which no Resident Indian citizen is a partner or shareholder,
- IV. Indian Income to be taken **pro rata** if all operations of a business not carried in India,

Explanation: “business connection” includes a person, who –

- I. holds or habitually exercises holds an authority to conclude contract on behalf of the non-resident, except for purchase of goods or merchandises,
- II. has no such authority but maintains stock of goods and merchandise in India, from which he regularly delivers stock or merchandise on behalf of the non-resident,
- III. Secures orders in India for the non-resident and other non-resident, controlling, controlled by or subject to the same common control as that of non-resident,

However, there will be no business connection as above, if a non-resident carries on a business through a broker, general commission agent or any other agent of independent status, acting in ordinary course of business.

For this purpose, a broker, general commission agent or an agent shall be deemed to be of an independent status, if he does not work mainly or wholly on behalf of the non-resident.

Further, no income deemed to accrue or arise in India to a foreign mining company (FMC) through or from the activities which are confined to display of uncut and unassorted diamonds in a Special Notified Zone

2. "Salary" earned in India i.e. salary payable for services rendered **in India**. It also includes salary paid for the rest period or leave period preceded and succeeded by services rendered in India and forms part of service contract of employment.
3. Salary received by **Indian national from the government** in respect of services rendered **out of India**. However, any allowance or any perquisite paid abroad is fully exempt from tax under Section 10(7).
4. Any **dividend paid by an Indian company** outside India.
5. **Interest** payable by:-
 - a. Government or a resident person, unless such interest is payable in respect of borrowed funds used for a business or profession carried out of India, or by a non-resident person on funds borrowed for the business or profession carried in India.
 - b. the permanent establishment in India of a non- resident assessee and engaged in the business of banking in India to such resident or its head office or any permanent establishment or any other part of such non-resident outside India.
6. **Royalty** payable by the government or a resident person unless such royalty is in respect of any right of property or services utilised for a business or profession carried out of India for the purpose of earning any income out of India or by a non-resident person in respect of any right of property or services utilised for the purpose of business or profession carried in India or for the purpose of earning any income in India).

Exception:

- (i) Royalties payable for the transfer of any data, drawings, etc. outside India or imparting of information outside India under an approved agreement by the Central Government made before the 1st day of April, 1976.
- (ii) Royalties paid In lump sum, by a resident for transfer of computer software, supplied by a non-resident along with

the computer or computer-based equipment under a scheme duly approved by Government of India

7. Fees for technical services payable by the government or a resident person, unless such fees are payable in respect of services utilised in a business or profession for earning any income out of India or by a non-resident person for services utilised in a business or profession carried on by him in India or for earning any income from any source in India..

Exception: fees are payable under agreement made before the 1st day of April, 1976 and approved by the Central Government.

The income of a non-resident is deemed to accrue or arise in India under any of the above clauses, shall be included in the total income of the non-resident, whether or not, the non-resident has -

- (i) a residence or place of business or business connection in India; or
- (ii) has rendered services in India.

Eligible Fund Managers in India will however not to constitute business connection of offshore funds as per an exception inserted vide section 9A.

6. RECEIPT VS. REMITTANCE

The “receipt” of income refers to the first occasion when the recipient gets the money under his control. Once an amount is received as income, any remittance or transmission of the amount to another place does not result in “receipt” at the other place.

7. ACTUAL RECEIPT VS. DEEMED RECEIPT

It is not necessary that an income should be actually received in India in order to attract tax liability. An income deemed to be received in India in the previous year is also included in the taxable income of the assessee. The Act enumerates the certain incomes which were dealt with earlier. E.g. If a resident holds an immovable property in Delhi and the rent received thereon is transferred to his bank account in Mauritius, the rent would still be subject to income tax though the income has not been received in India.

8. RECEIPT VS. ACCRUAL

Income is said to be received when it reaches the assessee; when the right to receive the income becomes vested in the assessee, it is said to accrue or arise.

9. BASIS OF CHARGE FOR DIVIDEND INCOME

Under the companies Act, 2013, a company can declare dividend only at its Annual General Meeting. Accordingly, U/s 8, dividend is deemed to be the income of the previous year in which it is declared irrespective of the fact when it was received by the shareholder. Hence the method of accounting for the dividend becomes immaterial for the purposes of this section.

But the position is quite the opposite in case of interim dividend, which is deemed to be the income of the previous year in which the amount of such dividend is unconditionally made available by the company to a shareholder irrespective of the date of declaration of interim dividend.

Deemed Dividend under S 2(22) is deemed to accrue or arise in the year in which it was paid or distributed.

This can be summarised as follows:

Final Dividend	Date of declaration
Interim Dividend	Date of distribution
Deemed dividend	Date of Distribution

Illustration-16:

Determine the scope of total income in respect of the following incomes if the assessee is a (1) resident or (2) a resident and ordinarily resident or (3) a resident but not ordinarily resident:

Income	Rs
Interest from U.S. Growth Bonds received in India	60,000
Interest from U.S. Growth Bonds received in U.S.	60,000
Interest from U.S. Growth Bonds received in U.S but remitted to India	60,000
Capital gain on house in Mumbai but sold in London	60,000
Capital gain on house in Mumbai but sold in Mumbai	60,000
Rent of a villa in Paris received in Paris	60,000
Rent of a villa in Paris received in Paris	60,000
Agricultural Income from Tea Gardens in Sri Lanka received in Sri Lanka	60,000
Agricultural Income from Tea Gardens in Sri Lanka received in Mumbai	60,000
Profit from a branch in Sydney	60,000

Profit from a branch in Mumbai	60,000
Salary for working in Jaipur received in Jaipur	60,000
Salary for working in Jaipur received in Lahore	60,000
Salary for working in Lahore received in Jaipur	60,000
Salary for working in Lahore received in Lahore	60,000

Solution

Particulars	R & OR	R & NOR	N R
Interest from U. S. Grawh Bonds U.S.A. received in India	60,000	60,000	60,000
Interest from U. S. Grawh Bonds U.S.A. received in U.S	60,000	—	—
Interest from U. S. Grawh Bonds U.S.A. received in U.S but remitted to India	60,000	—	—
Capital gain on house in Mumbai but sold in London	60,000	60,000	60,000
Capital gain on house in Mumbai and sold in Mumbai	60,000	60,000	60,000
Rent of a villa in Paris received in Paris	60,000	—	—
Rent of a villa in Paris received in Mumbai	60,000	60,000	60,000
Agricultural Income from Tea Gardens in Sri Lanka received in Sri Lanka	60,000	—	—
Agricultural Income from Tea Gardens in Sri Lanka received in Mumbai	60,000	60,000	60,000
Profit from a branch in Sydney	60,000	60,000*	—
Profit from a branch in Mumbai	60,000	60,000	60,000
Salary for working in Jaipur received in Jaipur	60,000	60,000	60,000
Salary for working in Jaipur received in Lahore	60,000	60,000	60,000
Salary for working in Lahore received in Jaipur	60,000	60,000	60,000
Salary for working in Lahore received in Lahore	60,000	60,000	60,000
Total	9,00,000	6,60,000	6,00,000

*if controlled from India

10. HEADS OF INCOME

10.1. Classification of income

Income tax is payable by an assessee on his total income from all the source of income. Each source has its own unique features and requires specific treatment for correct computation of income from that particular source. Naturally, rules and method for computation of income from each such source are different according to the nature of the source. These sources of income are classified under various heads of income in section 14. These heads of income are as follows:

- 1) Income under the head salaries (Section 15 – 17)
- 2) Income from house property (Section 22 – 27)
- 3) Profits & gains from business or profession (Section 28 – 44)
- 4) Capital gains (Section 45 – 55)
- 5) Income from other sources (Section 56 – 59)

10.2. Importance of different heads

Each head of income provides a different scheme of computation of taxable income under that head depending upon the nature of income and the complexities attached with that head of income. For this reason, each of the head of income has its own deeming provisions and provisions for exclusions and deductions and deductions of expenses etc.

It is therefore, necessary that an income belonging to a specific head must be computed under that head only. If an income cannot be placed under any of the first four heads, it will be taxed under the head “Income from other sources”.

Aggregate of net income under various heads gives total income of the assessee person, from which deductions are made under chapter VIA. The net result is called the total income or sometimes taxable income. Therefore, computation of income under different heads provides the starting point of determining the tax liability.

10.3. Heads to be mutually exclusive

All the heads of income are mutually exclusive. If any income is considered under a particular head e.g. Income from house property, it will not be taken into consideration for another head e.g. Profits and Gains from business and profession.

The nature of income is such that at times, it may not be possible to have water-tight compartmentalization.

Illustration 17

Under which head would the income of 3 offices are compositely let out on rent by alongwith services like intercom, security guard, telephone connection, furniture and fixtures, etc. of Swayam will be taxable ?

Solution

The rent in respect of the commercial property should be taxed under “Income from House Property”. However, income arising out of rentals of the other services should be taxable under the head “Income from Other Sources”. Alternatively, the entire income arising out of the property as well as the services could be taxable as “Income from Business or Profession”

As per departmental clarification, the income in respect of properties should be taxed as “Income from House Property” and the income out of rentals of the other services to be taxed under “Income from Other Sources”.

10.4. Tax on aggregate income under all the heads

Although the income is computed under five different heads of income, tax will be computed on the aggregate or total income from all the sources taken together at the prescribed rates. However, different tax treatment is given to different items. For instance, long-term capital gains (LTCG) are generally taxed at 20%. But LTCG on listed securities is exempt from tax. Similarly, short-term capital gain on sale of equity shares is taxed at 15%. The amount of such short-term capital gains would be deducted from the aggregate total income and accordingly tax rates are applied. Similarly, shipping companies are taxed based on tonnage of the shipping fleet. Lotteries, horse races etc. are taxed at the maximum rate of tax @ 30%. All such incomes are excluded and tax is computed on rest of the total income.

10.5. Common residential status for all the heads

Section 6 provides that where a person is resident for the purpose of any particular head of income, he will also be considered as resident for the purposes of computation of income under all the heads of income.

10.6. Separate sources of income under one head.

Income is classified for each head of income. Each head of income may have different sources of income falling under that head. For instance a person may be in receipt of his salary from more than one employer or rent from two or more house properties or more than one business. All such sources will be clubbed together to arrive at the income from that head.

10.7. Expenses under each head of income

It may be noted that expenses may be allowed under each head of income according to the provisions applicable. The recent trend is to restrict and standardize the allowance of expenditure. For instance virtually no expenses except

professional tax are allowed under the head salaries. Capital gains envisage deduction if only the cost of acquisition and improvement and transfer expenses and so on and so forth.

10.8. Expenditure incurred in relation to income not includible in total income

Section 14A provides that no deduction shall be allowed in respect of expenditure incurred by the assessee in relation to exempted income that is the income which does not form part of the total income under this Act

12. SELF ASSESSMENT QUESTIONS:

1. Why determination of residential status is important to ascertain the income tax liability?
2. Discuss the legal provisions in respect of residential status of an individual.
3. Briefly state the provisions for determination of the residential status of an (a) AOP (b) Firm (c) Company.
4. What is meant by the control and management of business?
5. When the income is deemed to accrue or arise or be received in India?
6. The incidence of income-tax depends upon the residential status of an assessee". Discuss.
7. Determine whether the following is true or false:
8. The business income received by X Ltd. an Indian company in New York is foreign income of X.
9. The dividend received from a foreign company in India is Indian Income
10. Write short notes on the following:
 - a. Income received in India
 - b. Income deemed to accrue or arise in India
 - c. Control and management of a business
11. Enumerate various heads of income.
12. State with reason that can an Income be computed under two heads of income.
13. How are the different heads mutually exclusive?
14. Would expenses in respect of collection of dividend be deductible from income from other sources?
15. Ascertain residential status for the assessment years 2017-18 and 2018-19, of Greg, an Australian citizen, came to India as a commentator during the following period:

From	To	Purpose
10.2. 2017	20-04-2017	World Cup
6-10-2017	25-12-2017	England Tour
04-01-2018	12-01-2018	Training Camp
02-03-2018	29-03-2018	Triangular Cup

Besides, Greg was in India for 340 days in four previous years from 2012-13, to 2015-16 260 days in three previous years from 2011-12 to 2013-14.

(Ans: 2015-16 Non-resident, 2014-15 R but RNOR)

16. Determine the residential status of Parthiv, who made his debut in international cricket on 11/03/2009. In the first match, he was injured and had to be hospitalized. In U.S. He was discharged from the hospital on 29/03/2010. He returned to India took over as coach for Indian cricket team visiting Pakistan. Parthiv submits the following details of his stay outside India :

From	To	Purpose/ Place
10-04-2017	28-04-2017	World Cup in Dhaka
03-05-2017	09-07-2017	England Tour
27-08-2017	10-09-2017	Canada Tour
11-09-2017	01-10-2017	US holidays
04-01-2018	26-03-2018	Pakistan Tour

(Ans: Non-Resident)

17. Ashok, an Indian citizen, leaves India on May 22, 2012 for vacation to Uganda and returns on April 9, 2018. Determine the residential status of X for the assessment year 2018-19.
(Ans: Non-Resident)

18. Determine the residential status for the assessment year 2018-19, of Sheila, a foreign citizen, who visits India since 1985 every year for a period of 100 days.

(Ans: Non-Resident)

19. Fletcher, a foreign citizen comes to India, for the first time on March 20, 2015. On September 1, 2015, he leaves India for Nepal on a business trip. He comes back on February 26, 2018 to permanently stay in India. Determine the residential status of X for the assessment year 2017-18 and 2018-19.

(Ans Resident and Not Ordinarily Resident for both the years)

20. Determine residential status for the assessment year 2018-19 of Marconi, an Italian citizen, who comes to India for the first time on May 28, 2016.

(Ans: Resident and Not Ordinarily Resident)

21. Determine the scope of total income in respect of the following incomes if the assessee is a (1) resident or (2) a resident and ordinarily resident or (3) a resident but not ordinarily resident

New York business income controlled from India	Rs. 100000
Mumbai Business Controlled from Paris	Rs. 40000
Salary in New York as Indian ambassador	Rs. 90000
Profit on sale of shop in Kolkata paid in Karachi	Rs. 50000
Acting in Indian film –fee received in Rome	Rs. 70000
Past untaxed profits remitted to India from London	Rs. 120000

(Ans. Resident 350000, R & OR 250000, R& NOR 350000/ past profits not taxable)

22. Blair, a French Citizen had the following incomes during the year ended 31/3/2018. Compute his Total Income for Asst. Year 2018-19 if he is a (1) resident or (2) a resident and ordinarily resident or (3) a resident but not ordinarily resident.

Income from House property in India	Rs. 30000
Income from property in Rome	Rs. 20000
Interest from Bank account in India	Rs. 2400
Income from business in Bangladesh controlled from India	Rs.32000
Interest from Bank account in U.S.	Rs. 22000
Salary earned and received in Tokyo	Rs. 24000
Income earned and received in London	Rs. 26000
Dividend from British Company received in India	Rs.34000

(Ans. Resident 19400, R&OR Rs. 98600 R but NOR Rs 66400)

23. Following are the particulars of income of X for the previous year 2017-18:

- i. X is employed in India and receives Rs. 24,000 as salary.
- ii. Dividend received in London on June 3, 2017: Rs. 31,000 from a foreign company;
- iii. Share of profit received in London on December 15, 2017 from a business situated in Sri Lanka but controlled from India:
- iv. Rs. 60,000; remittance from London on January 15, 2018 out of past untaxed profit of 2003-04 earned and received there: Rs. 30,000 and interest earned and received in India on May 11, 2018 Rs. 76,000.

Find out his gross total income, if he is (a) resident and ordinarily resident, (b) resident but not ordinarily resident, and (c) non-resident for the assessment year 2018-19.

(Ans: R&OR, his gross total income will be Rs. 105000 i.e. Rs. 24,000 + Rs. 31,000 + Rs. 60,000 R& N OR Rs. 84,000 i.e., Rs. 24,000 + Rs. 60,000). Non-resident, Rs. 24,000.

The remittance from London of Rs. 30,000 is not taxable it is not "receipt" of income. The interest of Rs. 76,000 earned and received in India is taxable 2015-16.)



SALARIES

(Sections 15, 16 & 17)

Synopsis

1. Introduction and Objectives
2. Basis of Charge
3. Meaning and characteristics
4. Scope of salary income
5. Tax Treatment of some receipts:
6. Taxable Value of cash allowances-
7. Taxable Value of Perquisites
8. Classification of Perquisites
9. Valuation of Perquisites
10. Profits in lieu of Salary
11. Deductions -Entertainment Allowance, Profession Tax
12. Practical illustrations
13. Self- Assessment Questions

1. INTRODUCTION AND OBJECTIVES:

This lesson explains “Salaries” the first and most important of the five heads of income given in section 14. Under the tax laws, concept of “Salaries” is very wide and includes not only the salary in common parlance but also various other receipts, gifts, perquisites and benefits. The lesson deals with various provisions what constitutes salaries and other relevant matters like salary, types of allowances , perquisites and benefits and their valuation for tax along with the applicable legal provisions contained in sections 15,16 and 17. Section 15 provides the basis of charging salary income and section 17 explains it. Section 16 prescribes the deductions to be made while computing the income from salary and explain the terms

2. BASIS OF CHARGE AND MEANING- Sec 15

2.1. Basis of charge

Section 15 provides that the following income shall be chargeable to income tax under the head "Salaries"—

- (a) any salary due from an employer or a former employer to an assessee in the previous year, whether paid or not;

(b) any salary paid or allowed to him in the previous year by or on behalf of an employer or a former employer though not due or before it became due to him;

(c) any arrears of salary paid or allowed to him in the previous year by or on behalf of an employer or a former employer, if not charged to income-tax for any earlier previous year.

Thus, the term salary embodies of past (arrears), present and future salary (Advance). However, where any salary paid in advance is included in the total income of any person for any previous year, it shall not be included again in the total income of the person when the salary becomes due.

Further, any salary, bonus, commission or remuneration, by whatever name called, due to, or received by, a partner from the firm shall not be regarded as "salary" for the purposes of this section because it is considered as business income u/s 28.

3. MEANING AND CHARACTERISTICS

Section 15 does not define the term salaries. It only says salaries –past, present and future will be taxable under the head “salaries”. Hence, it becomes necessary to determine, whether any particular income is to be taxed under the head “Salaries” or not. This is done with the help of common practices, tests, norms, yardsticks, criteria and essential characteristics to find out whether the income is taxable as salaries or not. These are discussed in detail as under: -

1. Employer-employee relationship:

Salary can be defined as the payment of remuneration by an employer to the employee for rendering personal services to the employer under an expressed or implied contract for rendering such services. From the definition the term salary implies the existence of the following conditions namely--,

- a) There are two parties – the employer and the employee.
- b) The parties have an agreement of employment.
- c) The agreement can be express or implied.
- d) Agreement is for rendering of personal services by the employee to the employer.
- e) In consideration of the services rendered, the employer makes payment of remuneration to the employee.

2. Compensation for services rendered :

Salary is paid as a compensation for the services rendered as an employee and not in any other capacity. E.g. remuneration paid by a hospital to a doctor employee for taking care of the patients in that hospital will be salary, but the services rendered by that doctor to patients in his private clinic will not be salary as he is not an employee of the patients.

Payment received from patients will not be salary but his professional income.

It will be true of services rendered by other professionals like doctors, architects; lawyers, chartered accountants etc. to their clients and the fee paid by their clients will be professional fees not salary.

Under Section 17, salary includes payments made in other forms like gift, perquisites etc.

3. Name or form not important:

Any remuneration paid as compensation for services rendered by an employee to his employer will be treated as salary regardless of name given such as salary or wages or otherwise so long as -

- the relationship between the payer and payee is that of employer and employee; and
- the payment is made as a compensation for the services rendered by the employee

4. . Mode of Payment

Salary may be paid in cash or kind.

5. More than One Source :

Salary may be from more than one employer.

6. Type of Employment:

Salary may be in any capacity like part-time employment or full time employment.

7. Past, Present and prospective employer

Salary may be received from not just the present employer but also a prospective employer and in some cases even from a former employer for example pension received from a former employer.

8. Real intention to pay :

Salary income must be real and not fictitious. There must exist an intention or an obligation to pay and `receive salary.

9. Subsequent Surrender of Salary not tax-free;

Salary is taxed on due basis. A subsequent surrender of the salary will not be tax-free except where an employee surrenders his salary to the central government, and then the salary so surrendered will not be treated as taxable income of the employee.

10. Tax- Free salary

Salary paid as tax-free is also taxable in the hands of the employee, though contractually income tax on such is borne not by the employee but by the employer.

11. Time of taxability;

Salary is taxable in the year of *receipt* or in the year of *earning or accrual* of the salary income, *whichever is earlier*. In simple terms following situations may arise :-

- Current salary will be taxable on accrual basis, as it will be payable later.
- Past salary or arrears will be taxable, when they are actually received, if they were not taxed earlier.
- Advance salary will be taxable at the time of receipt and it will not be taxed again when it is accrued.

As a result, salary is taxable at the time of accrual or receipt, whichever is earlier. Accordingly, method of accounting employed by the employee is not relevant to determine the taxability of salary.

12. Salary received by individuals only

Salary is taxable in the hands of individuals only because it is a compensation for personalised services, which can obviously be rendered by a normal human being only. No other type of person such as a firm, HUF, company or a body corporate can earn salary.

13. Voluntary payments taxable as salary

Voluntary payments like gift by an employer to an employee also form the part of taxable salary.

14. Salary in respect of services rendered in India

Under section 9 salary, leave salary and pension paid outside India are deemed to accrue and arise in India and are taxable in India. Similarly, salary paid to Indian diplomats by the Government of India is deemed to accrue and arise in India although the same is exempted u/s 10.

15. Gross salary Taxable;

Compulsory deductions from salary such as employees' contribution to provident fund, deduction for medical scheme or staff welfare scheme etc. are examples of instances of application of income. In these cases, for computing total income, these deductions have to be added back in the net salary received and gross salary will be taxable. .

4. SCOPE OF SALARY INCOME- SECTION 17

4.1. While, section 15 provides the scope and basis of salaries, section 17 explains it in an inclusive definition.

Salary includes:-

- a. Wages;
- b. Any Pension or Annuity;
- c. Any Gratuity;

- d. Any fees, commission, perquisites or profits in lieu of or in addition to salary or wages;
- e. Any advance of salary;
- f. Any encashment of leave salary;
- g. Annual accreditation to provident fund above the prescribed limits; and
- h. Any amount of credit to provident fund of employee to the extent it is taxable.

4.2. The term "salary" includes not only the basic salary but also fees, commission, bonus, taxable value of cash allowances and perquisites, retirement benefits, encashment of leave salary, advance of salary, arrears of salary, various allowances such as dearness allowance, entertainment allowance, house rent allowance, conveyance allowance, value of perquisites by way of free housing, free car, free schooling for children of employees, etc. Tax treatment of all such receipts is given later in this lesson.

5. TAX TREATMENT OF CERTAIN RECEIPTS

5.1. Basic Salary

Basic salary is the amount of salary fixed as per the terms of employment. It may be a pre-determined fixed sum, or a graded amount enhanced by pre-fixed annual increment. Under the graded system, the terms of employment fix the salary at say Rs.12000-300-15000-500-20,000. This means that the employee begins his job with a basic salary of Rs 12,000 per month. Which will be raised to Rs 12,300 p.m. after an annual increment of Rs. 300. The annual increment will continue till he reaches level of Rs 15,000 p.m. Thereafter, the annual increment will be Rs 500 per annum till he reaches level of Rs 20,000 p.m. Once his salary becomes Rs 20,000 p.m., his annual increment will be frozen. No further increment will be given thereafter, unless he is promoted and placed in other grade.

5.2. Fees, Commission and Bonus

Any fees, commission, bonus, or incentive paid or payable to an employee by an employer is taxable and is included in salary. Such Commission etc. may be payable as a fixed amount or as a percentage of turnover or partly fixed and partly as a percentage of turnover. When commission is based on fixed percentage of turnover achieved by employee, it is included in basic salary for the purpose of grant of retirement benefits and for computing, certain exemptions discussed later

5.3. Arrears of salary:

Arrears of salary are taxed on receipt basis, if the same has not been taxed earlier. However, the employee will be entitled to claim relief u/s 89 in respect of such arrears.

5.4. Advance Salary:

Salary received in advance is taxable on receipt basis in the year of receipt. There will be no tax again in the year in which the salary actually accrues. The employee can claim relief u/s 89 in respect of advance salary. It is important to note that salary received in advance is taxable not advance or loan against salary. For example, salary for three months is given in advance; it will be taxable when received. But loan or advance granted against three months' salaries will not be taxable.

5.5. Gratuity (Section 10(10)):

Gratuity is a lump-sum payment to reward an employee for his past services, on his retirement or termination. Amount received as gratuity on termination is exempt u/s 10(10) as under:-

- 1 Employees of Central or State governments or local authorities fully **exempt**
- 2 Employees in a concern covered under the Payment of Gratuity Act, 1972 is **exempt** subject to the lowest of the following amounts :

- a. Amount of gratuity received,
- b. Rs 10,00,000
- c. 15 days' salary for every completed or part thereof in excess of six months, year of service computed based on last salary drawn taking numerator of 26.

$$\frac{* \text{Completed year of service} \times 15 \text{ days} \times \text{Last Drawn Salary}}{26}$$

- 3 Employees in a concern NOT covered under the Payment of Gratuity Act, 1972 is exempt subject to the lowest of the following amounts :

- a. Amount of gratuity received,
- b. Rs 10,00,000
- c. Half month's salary for every completed year of service in excess of six months (ignoring the fraction) computed based on average salary of last 10 months preceding the retirement.

$$* \text{Completed year of service} \times \frac{1}{2} \times \text{Avg Salary for last 10 months}$$

[*Completed year of service includes a year or part thereof in excess of six months]

Illustrations -1

Ashik, a government servant, retires 1 June 2018 after 22 years and 9 months' service. He receives gratuity of Rs 15,00,000 . Determine the Determine the amount of exemption of gratuity if he was drawing a basic Salary for 10 months preceding the month of his retirement at Rs 40,000 p.m.

Solution

Since Ashik is a government employee, amount received as gratuity on retirement is fully exempt U/s 10(10).

Illustrations-2

In the above case, what will be the effect if Ashik was working with ABC Limited, covered under the Payment of Gratuity Act, 1972?

Solution:

Since Ashik is the employee of a private employer XYZ Limited covered under the Payment of Gratuity Act, 1972, exempt amount will be Rs 5,30,769 being the least of the following:

I. Actual amount received	15,00,000
II. Notified amount	10,00,000
III. 15-day's salary based on last drawn salary Rs.40, 000* 15/26 *23 years	5, 30,769
Taxable	9,69,231

Illustrations-3

In the above case, what will be the effect if ABC Limited is NOT covered under the Payment of Gratuity Act, 1972?

Solution:

Ashik is the employee of a private employer XYZ Limited not covered under the Payment of Gratuity Act, 1972. Exempt amount will be the lowest of the following:

I. Actual amount received	15,00,000
II. Notified amount	10,00,000
III. 15-day's salary based on last drawn salary Rs.40, 000 X (11) = 23*0.5 -fraction ignored)	4,40,000
Taxable	10,60,000

5.6. Commuted Pension (Section 10(10A) :

Pension is a regular payment made at monthly or annual intervals by an employer to his employee on retirement his retirement of an employer as a reward for his past services. When an employee is allowed to forgo a portion of pension in lieu of a lump sum amount called commutation of pension. Tax treatment of these two kinds of pension is as under:

- a) *Regular payment* of pension, monthly or quarterly or at some other interval, periodical or uncommuted pension is **fully taxable** in the hands of all employees, whether government or non-government.
- b) Lump sum payment received by an employee on commutation of pension as per service rules will be-

- i. *fully exempt* for employees of the Central or State Government or a Local Authority or a Statutory Corporation
- ii. partially exempt for other employees to the extent of -
 - a. *One half of the total value* of pension If the employee has not received any gratuity on termination of employment, and
 - b. *One-third of the total value* of pension, if the employee has received any gratuity on termination of employment.

Illustration-4

Determine the amount of taxable pension, if A receives a monthly pension of Rs 50,000 from the government.

Solution:

Regular monthly payment of pension received from government will be fully taxable.

Illustration-5

Determine the amount of taxable pension, if A receives a monthly pension of Rs 50,000 a private limited company.

Solution:

Regular monthly payment of pension received from government will also be fully taxable. It is immaterial who the employer is.

Illustration-6.

A retires from government service on 01/06/2017. He receives a pension of Rs 5000 p.m. till 31/12/2017. On 01/01/2018, A opts for commutation of 40 per cent of the value of his pension for a lump sum amount of Rs 1,20,000. After commutation, A gets Rs 3,000 per month being 60% of the total pension. Determine the taxability of pension if no gratuity is paid to A.

Solution:

- a) Lump sum amount of Rs. 1,20,000 received on commutation of pension will be exempt as A is a government employee
- b) Regular pension Received during the year 2017-18
Rs 44,000 *will be fully taxable

01/06/2017 to 31/12/2017 @ Rs 5,000 P.M= Rs 35,000

01/01/2018 to 31/03/2018 @ Rs 3000 p. m= Rs 9,000

Total Rs.44,000

Illustration-7

What will be the position in the above illustration, if A is a private employee?

Solution:**a. Commutation of Pension**

	Rs.
Amount Received on commutation of 40% of salary	1,20,000
Full Value of Pension = 1,20,000 /40%	3,00,000
Amount Received on commutation	1,20,000
$\frac{1}{2}$ of full value of pension Rs 3,00,000* $\frac{1}{2}$	1,50,000
Exempted Amount - being the lower of the two	1,20,000
Taxable Amount [1,20,000-1,20,000]	NIL

Regular pension of Rs 44,000 will be taxable irrespective of the fact that A is government employee or a private employee or whether or not he is in receipt of any gratuity.

Illustration-8

Ascertain the taxability, if A also receives Rs 50,000 as gratuity.

Solution:

- a. Regular pension of Rs. 44,000 fully be taxable in all cases.
- b. If A is a government employee, the amount received on commutation of pension will be fully exempt regardless of the fact that he also receives gratuity.
- c. If A is a non- governmental employee and is in receipt of gratuity and he receives Rs. 1,20,000 on commutation, he will be entitled to exemption of Rs 1,00,000 being 1/3 of full value of pension (1/3 of Rs 3,00,000). Balance Rs 20,000 will be taxable.

5.7. Encashment of Leave Salary {Section 10(10AA)}

When an employee, instead of enjoying leave at his credit, gets the same encashed, following tax treatment will be given:-

- a. Amount received on encashment of leave during the *continuity of employment by all the employees*, will be *taxable* in the year of receipt. However, the employee will be entitled to relief u/s 89.
- b. Amount received on encashment of leave at the time of retirement by way of *superannuation* or otherwise, will be-
 - i. *fully exempt in case of an employee of the Central or State Government* ; and
 - ii. Partially exempt in case of any other *employee including employees of a local authority or a statutory corporation* to the extent of the lowest of the following and only the balance will be taxable:-

- i. Actual amount received
- ii. Notified Amount currently Rs 3,00,000;
- iii. 10 months' average salary or
- iv. Cash equivalent of leave to be encashed
i.e. (Leave Entitlement - Leave Availed) X Average Salary

Other Points

- i. Salary for the purpose of calculating the exempt leave encashment means total of basic salary, dearness allowance and commission on sales achieved by salesmen.
- ii. Average salary means average salary of 10 months immediately preceding the retirement.
- iii. Leave entitlement is to be taken at 30 days for each completed year of service. *Part of the year will be ignored and not considered as completed year of service.*
- iv. If leave is encashed from more than one employer, the exemption limit will be taken in respect of all the employers.
- v. Superannuation means retirement on attaining a certain age e.g. 60 years. Courts have held that termination and even resignation of the employee will entitle them to exemption under this section.
- vi. Leave to the credit of the employee means total leave available as reduced by total leave availed.

Illustration- 9

A retires from his job with the Government of Maharashtra on 01/06/2016 after rendering services for 22 years and 9 months.

He was drawing a basic Salary for 10 months preceding the month of his retirement at Rs 8000 p.m.

Under the service rules, A was entitled to 2 months' leave for every year of service or part thereof against which A availed total earned leave of 10 months.

On Retirement, A received leave entitlement of Rs 2,88,000 i.e. 36 months @ Rs 8000p.m., worked out as :

Leave entitlement - 23 years @ 2 months = 46 months for every year of service or part thereof less-leave availed 10 months

Compute amount of exemption of encashment of leave salary

Solution:

Since A is a government employee amount, received as leave encashment on retirement is fully exempt U/s 10(10AA).

Illustration-10

What will be the exempt amount if A was employed with MSFC?

Solution:

MSFC is a statutory corporation not regarded as government. Hence, exemption would be at par with a private employee and worked out as the least of the following:

	Rs.
Amount Received on leave encashment	2,88,000
Notified Amount	3,00,000
10 months' average pay@ Rs. 8,000 p.	80,000
Encashment of unavailed leave 12 months	96,000
Exempted Amount - being the lower of the two	80,000
Taxable Amount [2,88,000-80,000]	2,08,000

**Leave entitlement – 22 months – Leave availed 10 Months ignoring fractional period of service of 9 months as it is not rounded off.*

Illustration-11

What will be the exempt amount, if A receives the leave encashment while in service?

Solution

Leave encashment during continuance of employment is fully taxable regardless of who the employer is.

Retrenchment compensation –Sec. 10 (10B)

Any compensation received by a workman at the time of retrenchment or closure or transfer of undertaking including change of management resulting in interruption of service is exempt fully if it is paid under a scheme of closure approved by the central government and in other cases, least of the following amounts would be exempt:

- Notified amount presently Rs. 5,00,000
- 15 days' average pay for every completed year of service or any part thereof in excess of six months
- Actual amount.

Other points;

- Compensation under a Voluntary Retirement Scheme is also exempt u/s1010C.
- Where an assessee has to pay higher tax on account of such lump sum receipts, he is entitled to relief u/s 89.
- If an assessee claims exemption under this section, then he can not claim relief u/s 89[1].

Illustration-12:

A workman was retrenched after 20 year and 10 months service His average salary was Rs 15,000 per month. He was paid Rs 1,80,000 as the retrenchment compensation. Calculate the exempt amount.

Solution

The exempt amount will be least of the following:

	Rs.
Actual Amount Received	1,50,000
Notified Amount	5,00,000
#10-1/2 months' average salary	1,42,500
Rs 15,000 per month	
Exempted (Lowest of the above)	1,42,500
Taxable (1,50,000-1,42,500)	7,500

(15 days for 20 years and 10 months rounded off to next number.

Relief u/s 89 not available if he claims the above exemption.

5.8. House Rent Allowance (Section 10-13A)

House Rent Allowance or HRA paid by the employer to the employee to meet the housing expenses of the employee, is exempt from tax U/s 10(13A) being the least of the following :

- HRA actually received.
- Rent paid by employee in excess of 10 per cent of salary during the previous year.
- 50 per cent of salary, if employee is residing in the 4 metro cities of Mumbai, Delhi, Chennai or Kolkata and 40 per cent of salary, if the employee is residing at any other place.

Salary for the purpose of calculating the amount of deduction from HRA means the aggregate of Basic Salary, Dearness Allowance and Commission received by salesman on sales achieved by him but it does not include other receipts such as overtime pay, conveyance allowance, etc.

In simple words, so long, the rent paid is upto 10% of the salary, no HRA will be exempt. It is only if the rent paid is more than 10 %, then the actual HRA may be exempt to the extent of 40% or 50% of the salary.

Illustrations-13:

Calculate the amount of HRA exempt U/s 10(13A) in respect of an employee residing in Mumbai who was in receipt of basis salary of Rs. 65,000 Dearness allowance of Rs. 35,000 and HRA of Rs. 25,000 and he paid the actual rent of Rs. 15,000 per annum.

Solution:

Exemption of HRA will be the least of the following:

	Rs.
Actual HRA Received	25,000
Rent paid in excess of 10 % of salary	5,000
15,000- {10 % (65,000+35,000)}	
50% of salary	50,000
Exempted (Lowest of the above)	5,000
Taxable (25,000-5,000)	20,000

Illustrations-14:

Compute the exempt HRA, if rent paid is Rs. 50,000.

Solution:

	Rs.
Actual HRA Received	25,000
Rent paid in excess of 10 % of salary	40,000
$50,000 - \{10\% (65,000 + 35,000)\}$	
50% of salary	50,000
Exempted (Lowest of the above)	25,000
Taxable (25,000-25,000)	NIL

Illustrations-15:

Calculate the amount of HRA exempt U/s 10(13A) in respect of an employee residing in Agra who was in receipt of basis salary of Rs. 65,000 Dearness allowance of Rs. 35,000 and HRA of Rs 60,000 and he paid the actual rent of Rs 50,000 per annum .

Solution:

	Rs.
Actual HRA Received	60,000
Rent paid in excess of 10 % of salary	40,000
$50,000 - \{10\% (65,000 + 35,000)\}$	
40% of salary	40,000
Exempted (Lowest of the above)	40,000
Taxable (60,000-40,000)	20,000

Note - The time and notified amounts , wherever applicable in this lesson, are technically not in syllabus but given to keep the text logically complete. These should be available in question.

6. TAXABLE VALUE OF CASH ALLOWANCES:

Most employers give different types of allowances or fixed monetary amounts to the employees over and above basic salary. These allowances are paid to meet some personal expenses like house rent, conveyance etc. or for performance of his duties such as entertainment or telephone allowance or partly for personal and partly for official purpose.

All such allowances are taxable and included in gross salary unless specific exemption is provided in respect of such allowance. Accordingly, the allowances are of four categories –

- Allowances, which are fully taxable;
- Allowances, which are wholly and unconditionally exempt;
- Allowance, which are tax-free or taxable subject to certain conditions or limits;
- Allowances, in respect of which exemption is allowed only for a sum prescribed on *ad hoc* basis.

Some of these allowances are dealt with as under.:-

6.1. Allowances Fully Taxable :

- a. **Dearness Allowance**, a compensatory allowance paid to meet high prices and increased cost of living.
- b. **City compensatory allowance** also a compensatory allowance paid to employees posted in big cities like Delhi, Mumbai to compensate the high cost of living in such cities
- c. **Non- practicing allowance** normally paid to compensate professionals in government service like doctors, chartered accountants, engineers, scientists etc, who are prohibited from doing private practice,
- d. **Warden or proctor allowance** paid in educational institutions for working as a warden of the hostel or as a proctor in the institution,
- e. **Deputation allowance** paid to an employee sent from his permanent place of service to some place or institute on deputation for a temporary period,
- f. **Overtime allowance** paid as extra wages paid to an employee putting in extra working hours over and above his normal hours of duty,
- g. **Servant allowance**, if paid in cash even if the employee may have employed servants.
- h. **Other allowances** by whatever name called such as family allowance, project allowance, marriage allowance, education allowance, holiday allowance etc. as these allowances are not specifically exempt.

6.2. Wholly and unconditionally exempt Allowances

- a. Allowances paid to Judges of the High Courts and the Supreme Court,
- b. Allowances paid by the United Nations organization to its employees.
- c. Foreign allowance paid by the government to its employees being Indian citizen posted out of India for rendering services abroad
- d. Pension to gallantry award winners like Paramvir Chakra, Mahavir Chakra, Vir Chakra etc - S. 10(18)

6.3. Wholly or partly tax-free Allowances:

Following allowance are wholly or partly tax -free. Some of the exemptions are conditional. Most of the conditions and monetary limits, though prescribed in rules are incorporated in brief to make the subject comprehensive. Brief description of these allowances is as follows

a. Entertainment allowance- S.16 (ii)

Entertainment allowance the private sector employees for entertaining the business relations and clients of the employer is

fully taxable by even if the entire amount may have been spent by them.

For the Government employees, the allowance is partially exempt by way of deduction u/s 16(ii) upto 20 per cent of basic salary, or Rs. 5,000 per annum, whichever is lower. Full amount is first included in the salary and then the exempted amount is reduced.

b. Fixed medical allowances

Fixed medical allowance is taxable but reimbursement of medical expenses is exempt upto Rs 15,000

c. Tiffin / lunch allowance

Tiffin / Lunch Allowance paid in cash is fully taxable but Cost of lunch provided to employees on their work place or even lunch coupons redeemable with restaurants is a tax-free perquisite subject to fulfillment of certain *conditions prescribed by the CBDT*.

d. Transport allowance- Sec. 10(14)

Any allowance or benefit given to meet the expense wholly and necessarily in the course of employment is fully exempt u/10(14) subject to the assessee presenting the proof in this regard.

Under Rule 2BB ,Transport or conveyance allowance paid to meet conveyance expenses of the employee from place of residence to place of work and back is exempt upto Rs 1600 per month (Rs 3,200 in case of a handicapped employee) .

For example, if A is in receipt transport allowance @ Rs 2,000 per month, Rs 400 per month (Rs 2000-Rs 1,600) will be included in total income of A

e. Other allowances for official purposes-Sec. 10(14) ;

U/s 10(14) allowances (other than conveyance between residence and office) are exempt to the extent of amount actually spent from those allowances by the employee in meeting the official expenses.

For example, where an employee receives uniform allowance of Rs 5000 and spends Rs 4000 on uniforms, then Rs 4,000 actually spent will be exempt and unspent sum of Rs. 1,000 will be taxable in the hands of the employee.

Some other examples of the allowances paid for meeting expenses incurred exclusively in performance of official duties are travelling allowance, daily allowance, conveyance allowance, helper allowance, research allowance.

f. Education allowance:

Education Allowance given to meet the education expenses of the employee's is taxable in hands of employee. However, under rule 2BB a sum of Rs. 100 per month per child

per year (Rs. 300 if the child stays in a hostel) subject to maximum of two children is allowed as exemption from such allowance received by the employee.

g. Out of station allowance

An allowance granted to an employee working in a transport system to meet his personal expenses in performance of his duty in the course of running of such transport from one place to another is exempt upto 70% of such allowance or Rs.6000 per month, whichever is less.

7. TAXABLE VALUE OF PERQUISITES

7.1. Definition and Meaning of Perquisites:

Under section 17(2), value of perquisites allowed to an employee is chargeable to tax. But the section does not define the term. In normal commercial parlance, perquisites denote any casual emoluments or benefits attached to an office or position in addition to salary or wages. Perquisites are normally allowed in kind - not in cash; and are measurable in monetary terms.

7.2. Taxability of perquisites:

Perquisites are included in taxable salary only if they are:

- allowed by an employer to an employee,
- allowed during the continuation of employment,
- directly dependent on service,
- resulting in personal advantage to the employee; and
- derived by virtue of employer's authority.

7.3. Taxable perquisites

Sec. 17 (2) provides the following list of taxable perquisites:

- i. Value of *rent-free accommodation* provided to the employee by the employer.
- ii. Value of *concession in rent* in respect of accommodation provided to the employee by his employer.
- iii. Value of any *benefit or amenity* granted free of cost or at a concessional rate in any of the following cases:
 - a) by a company to an employee who is a director thereof
 - b) by a company to an employee who has substantial interest in the company
 - c) by any employer to an employee who is neither is a director, nor has substantial interest in the company, but his monetary emoluments under the head 'Salaries' exceeds Rs.50,000.
- iv. Any sum paid by the employer towards any obligation of the employee
- v. Any sum payable by employer to effect an assurance on the life of assessee

- vi. The value of any other fringe benefit given to the employee as may be prescribed.

7.4. Classification of Perquisites

As per section 17(2), perquisites are of three broad categories :

- Perquisites taxable in all cases
- Perquisites not taxable at all
- Perquisites taxable only in the hands of specified employees only

A. Perquisites taxable in all cases:

The following perquisites are taxable u/s 17(2) in the hands of all type of employees, whether specified or not:

1. Value of Rent free house provided by employer
2. Value of house provided at concessional rate
3. Any obligation of employee discharged by employer e.g. payment of club or hotel bills of employee, salary to domestic servants engaged by employee, payment of school fees of employees' children etc.
4. Any sum paid by employer in respect of insurance premia on the life of employee.

B. Perquisites, which are tax-free for all the employees

Section 17 specifically states that the following will not be taxable in the hand of the employees :-

a. Medical benefits within India :

Exempted medical benefits within India, include:-

- i. Medical treatment provided to an employee or any member of his family in a hospital maintained by the employer.
- ii. Any sum paid by the employer in respect of any expenditure incurred by the employee on medical treatment of himself and members of his family:
- iii. In a hospital maintained by government or local authority or approved by the government for medical treatment of its employees.
- iv. In respect of the prescribed diseases or ailments in any hospital approved by the Chief Commissioner.
- v. If the ordinary medical treatment of the employee or any member of his family is done at any private hospital, nursing home or clinic, the exemption is restricted to Rs.15000.

b. Medical benefits outside India

Exempted medical Treatment outside India includes :

- i. Any expenditure incurred by employer on the medical treatment of the employee or any member of his family outside India.

- ii. Any expenditure incurred by the employer on travel and stay abroad of the patient being the employee or member of his family and one attendant who accompanies the patient in connection with such treatment, shall be exempt to the following extent :
 - (i) The expenditure on medical treatment and stay abroad shall be exempt to the extent permitted by the Reserve Bank of India.
 - (ii) The expenditure on travel shall be exempt in full provided the gross total income of the employee (including this expenditure) does not exceed Rs. 2,00,000.

c. Medical Health Insurance within India

Exempted perquisites in respect of medical Health Insurance include:-

- i. Premium paid by the employer on health insurance of the employee under an approved scheme u/s 36(1)(ib)
- ii. Premium on insurance of health of an employee or his family members paid by employer on any scheme approved u/s 80D (Mediclaime).

d. ESOP or Sweat Equity

Any benefit provided by a company free of cost or at a concessional rate to its employees by way of allotment of shares, debentures or warrants directly or indirectly under any Employees Stock Option Plan or Scheme *ESOP/ESOS* of the company offered to such employees in accordance with the guidelines issued in this behalf by the Central Government. However, the difference between the fair Market Value and the issue price will be treated, when such equity is issued at concessional price, as the taxable perquisite value of ESOP

e. Transport

Amenity or benefit granted or provided free of cost or at concessional rate for use of any vehicle provided by a company or an employer for journey by the assessee from his residence to his office or other place of work, or from such office or place to his residence,

f. Refreshments

Refreshment provided by an employer to the employee during working hours in office environment.

g. Others:

- a. Value of Leave Travel Concession in India.
- b. Amount spent by the employer as its contribution to staff welfare schemes.
- c. Laptops and computers provided for personal use.

- d. Rent free official accommodation provided to a Judge of High Court or Supreme Court or an official of Parliament including Minister and Leader of Opposition in Parliament.
- e. Recreational facilities extended not to a particular employee but to a class of employees.
- f. Amount spent on training of employee or fees paid for refresher course.
- g. Telephone provided to an employee at his residence.
- h. Goods manufactured by the employer sold to employees at concessional rates
- i. Allowances to employees of UNO

Since FBT has been discontinued, value of cars and other perquisites will be taxable in the hands of the employees.

C. Perquisites taxable by specified employees only

U/s 17(2)(iii) the value of any benefit or amenity granted or provided free of cost or at concessional rate specified employees only will be taxable. Specified employee means an employee who is-

- *a director* of the employer; or
- who has a *substantial interest* i.e. more than 20 % voting power in the company; where he is employed or
- any other employee (of any employer including a company) whose income under the head salaries *exceeds fifty thousand rupees*

Salary for this purpose means salary due from, or paid or allowed by, one or more employers, exclusive of the value of all benefits or amenities not provided for by way of monetary payment,

The taxable perquisites are:-

1. Free supply of gas, electricity or water supply for household consumption;
2. Free or concessional educational facilities to the members of employee's household;
3. Free or concessional transport facilities;
4. Sweeper, watchman, gardener, personal attendant; and
5. Any other benefit or amenity.

7. VALUATION OF PERQUISITES:

Perquisites are benefits granted in kind. Hence, monetary value of the perquisites taxable in the hands of the employee is

required to be determined. Broad principles for determining the value of taxable perquisites are stated as under:-

- a) The amount actually spent by the employer will be the taxable value of perquisite allowed entirely for personal benefits of the employee.
- b) Taxable value of the perquisite allowed to an employee for official purposes only shall be nil and perquisites will not be taxable in the hands of employee.
- c) Taxable value of the perquisites allowed partly for personal and partly for official purpose, will be an amount of perquisites reasonably used for personal purposes.

Though the actual valuation rule are beyond the scope of the syllabus, general principles for valuation of perquisites may be considered.

a. Accommodation & Furniture

Valuation of furnished and unfurnished accommodation is made according to Valuation Rules. If the employer owns the furnishings, then 10 per cent of the cost will be added to the value of accommodation.

b. Transport

Broadly, no perquisite value is taken in the hands of individual employees in case where :-

- common transport such as bus provided to all the employees; or
- the employer is in the transport business; or
- a car is provided only for official use or for the purpose of travel from residence to office.

In other cases, a reasonable cost of such transport facilities will be treated as taxable value of perquisites in respect of such facilities

In case of a car owned by the employer is provided to an employee exclusively for his personal uses, the taxable amount will be determined by taking reasonable expenses incurred by the employer on the car maintenance and depreciation on the car as per income tax rules.

If such car is used both for private and official purposes, then a reasonable proportion of the perquisite value relatable to the personal use will be taken as the taxable value of the car perquisite in the hands of the employee.

c. Domestic servant

Salary of domestic servants of employer paid by the employer, perquisite value will be taken as per rules.

d. Gas, water or electricity:

- i. *Taxable perquisite* of providing supply of gas, water, or electricity will be nil, if the employer himself is engaged in the business providing these facilities.
- ii. If the employer is not in the business of supply of gas, water or electricity, then the amount spent by the employee in providing the facilities to the employee will be the taxable value of perquisites in the hands of the employee provided the entire facilities are for the personal use of the employees only. Any amount recovered from the employee will be reduced from the perquisite value.
- iii. Where the connection for gas, electricity, water supply is in the name of employee and the bills are paid or reimbursed by the employer, it is an obligation of the employee discharged by the employer. Such payment is taxable in case of all employees under Section 17(2)(iv)

e. Educational facilities:

- i. Taxable perquisite value of education provided by an employer being a school, college or educational institution will be nil.
- ii. If the employer is not a school, college or educational institution, but is engaged in some other business or profession, the value of school fees or colleges fees of the children of the employee paid by the employer will be the taxable value of perquisites in respect if such facility.
- iii. If the children of the employee are allowed free education in an institute run by the employer where the employer is engaged in other activities, then the value of the perquisites is reasonable cost of education and deemed by the income tax officer in the hands of specified employees.

f. Medical facilities

- (i) A sum up to Rs 15000 paid by the employer to the employee by way of reimbursement of medical expenses of the employee and his family will be exempt perquisite in the hand of the employee. Any payment made in excess of Rs15000 will be taxable.
- (ii) If the treatment is taken in a government approved hospital or recognized hospital, or in government hospital, no value will be taken as the perquisite value in respect of such medical treatment reimbursement.
- (iii) If the medical treatment is done outside India, then up to the amount approved by the RBI for such treatment, no perquisite value will be added to the taxable income of the employee. If payments made by the employer to the employee in this connection exceed the amount approved

by the RBI, then such excess will be treated as taxable salary in the hands of the employee.

- (iv) If the employer himself is a medical institution, provision of medical facilities will not attract any tax in the hands of the employee.

In other words, if an employer's own institution provides transport, education or medical facilities, there will be no taxable perquisite value in the hands of the employee.

8. PROFITS IN LIEU OF SALARY – S 17(3)

U/s 17 (3), profit in lieu of salaries includes:

1. Compensation for Termination of Employment or modification of Terms & Conditions

The amount of any compensation due to or received by an assessee from his employer or former employer at or in connection with the termination of his employment or the modification of the terms and conditions relating thereto;

2. Payment from Employer from PF or Other Fund

Any payment (other than any pension, gratuity, HRA, Retrenchment compensation, etc) due to or received by an assessee from an employer or a former employer or from a provident or other fund, to the extent to which it does not consist of contributions by the assessee or interest on such contributions.

3. Keyman Insurance Policy

Any sum received under a Keyman insurance policy including the sum allocated by way of bonus on such policy.

4. Sums Received from Future or Former Employer

Any amount due to or received, whether in lump sum or otherwise, by any assessee from any person -

- (A) before his joining any employment with that person or
- (B) after cessation of his employment with that person.

5. Payment of Employee's Obligation Employer

Any sum paid by the employer in respect of any obligation which, but for such payment, would have been payable by the assessee;

6. Payments from Certain Funds :

Any sum payable by the employer, whether directly or through a fund, other than a recognised provident fund or an approved superannuation fund or a Deposit-linked Insurance Fund established u/s 3G of the Coal Mines Provident Fund and Miscellaneous Provisions Act, 1948 or u/s 6C of the Employees Provident Fund and Miscellaneous Provisions Act, 1952 to effect

an assurance on the life of the assessee or to effect a contract for an annuity;

7. Treatment of Annual Accretion to Provident Fund;

Provident Funds are established to provide for the retirement benefits of the employees. The Scheme of funds envisages annual contributions from both the employer and the employee and the accumulation of interest on the balances. The funds are of three types, Viz.

- i. Statutory Provident Fund set up or established and administered by the Government.
- ii. Recognised Provident Fund set up by others but recognised by the Commissioner of Income Tax
- iii. Unrecognised Provident Fund set up by others but not recognised by the Commissioner of Income Tax due to non-compliance with the guidelines laid down for recognition.

The above position is summarised in the following table:

Tax Treatment under Different Provident Fund Schemes(PF)			
Type of Fund	Employer's Contribution	Interest on PF	Payment on Retirement
Statutory	Exempt	Exempt	Exempt
Recognised	Exempt upto 12% of Basic Salary (Excess taxable)	Exempt up to 8.5% p.a. (Excess taxable).	Exempt subject to rules
Unrecognised	Exempt	Exempt	Employers' Contribution & interest taxable –S 17(3).

Other Points:

1. Employer's Contribution to all the three funds is exempt at the time of contribution.
2. If the P.F. is deducted from the salary of the employee, salary will have to be grossed up in all the three cases.
3. Employees' Contribution when received back on retirement is exempt in all the three above mentioned cases.
4. Interest on Employees' Contribution from Unrecognised Provident Fund will be treated as Income from Other Sources.

8. Transferred Balance: - Sec. 17

When an unrecognised provident fund is subsequently recognised, the balance standing in the unrecognised provident fund are transferred to the Recognised Provident Fund is called transferred balances and deemed to be the salary income of that year as per section 17 (1). Such amount to the extent such

balance comprises of employees' contribution in excess of 12% of basic salary and interest credited in excess of 8.5% p.a.

9. DEDUCTIONS FROM SALARIES: - SECTION 16

From the aggregate of taxable amounts chargeable as taxable salary viz. salary, bonus, allowances and perquisites (called gross salary), income under the head "Salaries" shall be computed after making the following deductions u/s 16, namely:—

a) Entertainment Allowance

A deduction in respect of any entertainment allowance specifically received by a government employee, a sum equal to one-fifth of his basic salary or Rs. 5,000 whichever is less;

b) Profession Tax:

A deduction of any sum paid by the assessee on account of a tax on employment (profession tax) leviable by or under any law by the state government. .

Other than that, no further deductions are allowed under this head.

10. ILLUSTRATIONS

Illustration-16:

R, a Chartered Accountant was appointed as Finance Manager with ABC Bank on 1/4/2009 in the Salary grade of Rs. 12000 – 500 – 20000 – 1000 – 30000.

He was entitled to Leave Travel Concession for proceeding on leave of Rs. 4000. His actual expenditure on this account amounted to Rs. 5000.

As the bank is situated at a place where home food is available, R was offered Tiffin Allowance Rs. 6000, His actual lunch expenses amounted to Rs.10,000

Reimbursement of medical expenses for treatment of R and his family in private clinic was Rs. 50,000

The Bank has provided free unfurnished flat at Mumbai (rent paid by Bank: Rs.80,000). However, the perquisite value of that Flat was Rs. 30000.

The employer provided two watchmen (salary Rs. 2000 per month each).

Free use of Santro car for official use, car can be used for journey between office and residence.

Free refreshments provided at place of work (Rs. 100 per day for 200 days).

Compute Salary Income for the assessment 2018-19

Solution:**Computation of Salary Income R for AY 2018-19**

Particulars	Rs.
Basic salary (Rs 12,000 + 8 increments of Rs 500 p.m.)	1,92,000
Leave Travel Concession (Exempt)	NIL
Tiffin Allowance (Taxable)	6,000
Medical Expenses Reimbursed (50000 – 15000)	35,000
Rent Free Accommodation (Given)	30,000
Watchmen's Salary (2000 * 2 *12)	48,000
Santro Car only for Office use	NIL
Free Refreshments at workplace	NIL
Taxable salary	<u>3,11,000</u>

Illustration -17:

X is in negotiation with two employer A &B, who have made the following offers to X. Help him in making an appropriate choice.

Particulars	Rupees	
	A	B
Basic Salary	500000	50,0000
HRA – Actual Rent Rs. 200000	25,0000	0
Free House –fair rental value 50000	0	250000
Transport Allowance	100000	0
Free Use of Car – Amount spent		100000
Education Allowance for one child	5,0000	0
Free Education for 1 child. Amount spent	0	50000
Gardener Allowance	60000	0
Gardener's salary paid by employer		60000
Salary	960000	960000

Solution**Taxable salary from employer A**

Basic Salary		500000
HRA (Actual)	250000	
Less : Exempt	<u>150000</u>	100000
(HRA or 50 per cent of salary or Rent paid less 10 per cent of salary 200000- 10% of 500000)		
Education Allowance	50000	
Less : Exempt (100*12)	<u>1200</u>	48800
Gardener Allowance		60000
Transport Allowance	100000	
Less : Exempt (800*12)	<u>9600</u>	90400
Taxable Salary		<u>799200</u>

Taxable salary from employer B

Basic Salary	500000
Value of Free House	50000
Free Education for 1 child	50000
Gardener's Salary(120 * 12)	1440
Free Car	100000
Taxable Salary	851440

Taxable salary will be less with B, He should be preferred to A.

Illustration- 18:

XY Ltd offers a job with following options to M, who is neither a director nor he has substantial interest in the company:

PARTICULARS	I	II
	Rs.	Rs.
Basic Salary	1,70,000	1,70,000
Bonus	6,000	6,000
Education Allowance for 2 children	10,200	--
Education facility for 2 children in an		
Institution maintained by the employer	--	10,200
Sweeper Allowance	10,000	--
Free Sweeper	--	10,000
Entertainment Allowance	6,000	--
Club Facility	--	6,000
Conveyance Allowance for personal use	12,000	--
Free Car Facility for Personal Use	--	12,000
Medical Allowance	18,000	--
Medical Facility for M and Family Members in own hospital	--	18,000
Free gas, electricity and water supply	--	4,500
Fair Rent Rent-free unfurnished house:	24,000	24,000

Which option M must choose on the assumption that he and XY LTD will both contribute 10% of salary towards unrecognised PF?

SOLUTION:

PARTICULARS	I	II
	Rs.	Rs.
Income from Salary		
Basic Salary	1,70,000	1,70,000
Bonus	6,000	6,000
Education Allowance (10,200 - 2,400)	7,800	Exempt
Education Facility	--	Exempt
Sweeper Allowance/Facility	10,000	--
Entertainment Allowance/Club Facility	6,000	6,000
Conveyance Allowance/Car Facility	12,000	Exempt
Medical Allowance/facility	18,000	--
Allowance for gas/electricity/water/free facility	4,500	--
Rent free unfurnished house	13,430	7,600
Gross Salary	2,47,730	1,89,600

Taxable income is lower in option II, it should be preferred.

11. SELF ASSESSMENT QUESTIONS

1. What is Salary?
2. Discuss the difference profits in lieu of salary and perquisites.
3. Discuss various deductions available under the head salary.
4. Discuss the tax treatment of the perquisites for different employees.
5. Non- specified employees pay less tax than specified employees". Comment.
6. Rajesh is an employee of ABC Ltd. Since 1997, he is receiving entertainment allowance of Rs. 500 p.m. He submits following further information as on 31.03.2016 with the request to compute his taxable salary.
 - a) Net Salary of Rs. 4,000 p.m. (including entertainment allowance of Rs. 500 p.m. but after deducting income tax Rs. 500, Provident Fund Rs. 500 and Profession tax Rs. 70)
 - b) He is provided car for his exclusive use during office hours for office work. The petrol and other maintenance expenses come to Rs. 12,000 p.a.
 - c) Receives Leave travel concession for himself and his family for proceeding on leave to hometown of Rs. 5,000 as prescribed, while actual amount spent by him was Rs. 3,500.
 - d) During the year, he received free services of a cook. (Cost to the employer Rs. 4,400)
 - e) Received Rs. 8,000 on encashment of leave to his credit.

7. Rita was an employee of R India Ltd since 1968 covered by the Payment of Gratuity Act, 1972, retired on 31 January 2018 after 35 years and 7 months' service. At the time of retirement her employer paid gratuity of Rs. 65,000 (exempt u/s 10(10) Rs. 51,000). She received Rs. 50,000 being the accumulated balance of recognised Provident Fund. The due date of salary etc was 1st day of the next month and were paid on due date. She was entitled to a monthly pension of Rs. 400 with effect from 1st day of February 2018, which becomes due on the last day of the month. Compute her taxable income for A.Y.2018-19

8. Compute the taxable income of Hitesh for the AY 2018-19 on the basis of the following further information:

- (A) Basic Salary Rs. 2,5000 p.m.
- (B) House Rent Allowance Rs. 4000 p.m. Taxable value is 50% of the amount received.
- (C) Project Allowance paid during the year Rs. 12,000.
- (D) Bonus paid during the year Rs. 3,6000.
- (E) In retirement, on encashment of earned leave at his credit of 15 months he received Rs. 37,500. (Exempt u/s 10(10AA) Rs. 24,600)

9. Suhas submits the following information pertaining to the year 31.3. 2018 and asks you to compute his income from salaries for the AY 2018-19.

- a) Basic Salary Rs. 5,000 p.m.
- b) Dearness Allowance Rs. 3,000 p.m.
- c) Bonus @ 20% on salary plus Dearness Allowance
- d) Employee contribution 12.5% of basic salary+DA to RPF. Employer also contributes an equal sum.
- e) Interest on balance credited to his RPF @ 14% p.a. Rs. 17,500
- f) House Rent Allowance Rs. 10,000 p.a.
- g) Profession tax paid by employee Rs. 840.

He retired from services on 31.3.2018 opting for 60% commutation of pension and received Rs. 2,40,000 as the only terminal benefit.



INCOME FROM HOUSE PROPERTY (SECTIONS 22- 27)

Synopsis:

1. Introduction and objectives
2. Basis of Charge
3. Deemed owner
4. Income Exempt U/s 10
5. Computation of income from house property
[GAV, NAV SOP, deemed let out partly let-out and partly self-occupied Co-owneRs.hip, deductions]
6. Miscellaneous- ArreaRs. , Losses , TDs and no other deductions
7. Illustrations
1. Self - Examination Introduction and Objectives

1. INTRODUCTION AND OBJECTIVES:

Income from house Property” is significantly different from the other heads of income unlike the other heads as it covers not only the actual income but also the notional income.

This lesson explains the complex provisions related to “Income from house property”.

2. SCOPE AND BASIS OF CHARGE: S. 22

2.1 Sections 22 to 27 prescribe the law in relation to taxation of income from house property. Brief gist of these provisions is as follows :

- Section 22 defines the scope of Income from House Property.
- Section 23 gives the mode of computation of income,
- Section 24 specifies the amounts deductible therefrom.
- Section 25 deals with the amounts not deductible.
- Section 26 deals with the income of co-owneRs. of a property.
- Section. 27 gives the cases where a peRs.on not being an owner of the property will be taxed as the deemed owner of such property.

2.2 Section 22 provides that Annual Value of property consisting of **any building or lands appurtenant thereto** of which the **assessee is the owner**, shall be chargeable under the head Income from House Property.

The section specifically excludes property occupied for the purpose of assessee's own business or profession.

2.3 An analysis of the section brings about the following attributes to attract chargeability under the head the income from house property. :-

(a) The head "income from house property" extends to a property being a building or land appurtenant or adjacent thereto.

'Building' means any habitable four-wall structure covered by a roof. It is immaterial whether the building is residential or commercial such as warehouse, office or factory godown, wedding hall, auditorium, business centre, etc.

'Land appurtenant' means the land connected or adjacent to the building e.g. open space, approach roads, courtyard, compounds, courtyards, backyards, playgrounds, parking spaces, etc.

(b) Income from any other property e.g. rental Income from a vacant plot of land is not chargeable to tax under this head unless it is appurtenant to a building.

(c) The assessee owns the property. It is only the owner or deemed owner of house property who is liable to tax on income under this head.

Following points are important in this regard:

(i) Any person may be the owner whether an individual, HUF, firm, company, cooperative society or an association of persons.

(ii) Such person is the owner of the property in the previous year. Any subsequent change in the ownership of the property is immaterial.

(iii) A tenant is not the owner of a property. Hence, income of a tenant from sub-letting a rented property to another tenant is also not covered under this head. It will be taxable as business income or income from Other Sources.

(d) The property is either let-out or used for own residence. The section specifically excludes a property used for assessee's own business or profession.

3. DEEMED OWNER- SECTION. 27

Section 27 provides exceptions to the principle that own per Rs. hip as the basis of charging income under the head ‘income from house property’ The section states that following classes of per Rs. on shall be deemed to be the owner of a property although they may not be the legal owner thereof.

a) When an individual transfer Rs. any property to **his spouse or a minor child** other than a married daughter for inadequate consideration, such individual shall be treated as deemed owner of that property.

In such cases, the legal owner of the property is the spouse or the minor child; still the transferor shall be treated as owner for the purpose of charging income under the head income from house property.

b) The holder of an **impartible estate** is deemed to be the owner of the entire property. E.g., an HUF jointly holding a property on behalf of all its member Rs. shall be deemed to be the owner of such property although the property may be in the name of an individual member of family.

c) A **member of co-operative society, company or other association of per Rs. on** to whom a building has been allotted under a house building scheme of society will also be deemed to be the owner of that property.

d) A purchaser, who has received possession of a property in part performance of a contract within the meaning of **section 53A of the transfer of property Act** is deemed to be the owner of that property despite the fact that the agreement for buying of property has not been registered with the appropriate authority.

e) A per Rs. on being a lessee, who has acquired right by way of long-term lease of property for period of more than 12 year Rs., is deemed to be the owner of such property and income from that property will be chargeable as the income from house property. This provision is not applicable on any right by way of a lease renewable from month to month or for a period not exceeding one year.

4. HOUSE PROPERTY INCOME EXEMPT U/S 10

Section 10, 11 & 13 prescribe exemptions in respect of Income from house property of certain institutions, organisations or peRs.ons or in certain circumstances. Some of such exemptions are as under:-

- (a) A farmhouse used for agricultural purpose section- 10(1)
- (b) Income of one Palace of an ex- Ruler - section 10(19A)

- (c) A local authority section -10(20)
- (d) A scientific research association -section 10(20),
- (e) An Institution for development of Khadi & Village Industries - section 10(23BB)
- (f) Khadi & Village Industries Board -section 10(23BB)
- (g) A body for administration of charitable & religious trusts & endowments -section 10(23BBA)
- (h) Approved funds, educational institutions or hospitals-section 10(23C),
- (i) A trade union or association of trade union - section 10(24)
- (j) Resident of Ladakh district -section 10(26A)
- (k) Statutory corporations/ other institution or association finance by the government for promoting the interests of the members. of the scheduled caste and scheduled tribes-section 10(26B)
- (l) Co-operative society for promoting the interests of the members. of the scheduled caste and scheduled tribes-section 10(27)
- (m) A Property held for charitable purposes -section 11
- (n) A political party -Section 13)

Besides , Under Section 22 , a property used for own business or profession such as letting out property to paying guest, employees' quarter Rs., residence of partner Rs. or director Rs. is excluded from the income. If such property yields any income, it will be chargeable as business income and not house property income.

U/s 23(1) One Self Occupied Property of an individual or a HUF assessee is exempt. This benefit is not available to a property which is let out nor to non-living entities like firms, companies, etc.

5. COMPUTATION HOUSE PROPERTY INCOME:

Section 23 lays down the methodology for computing the income from house property. Under the section, first step is to determine the annual value of the house property.

Section 24 provides for deductions to be made from the annual values determined u/s 23,

These provisions are explained below:

5.1 Annual Value -Section 23

Section 2(22) defines annual value "as the annual value determined under Section. 23. The section assigns no definitive meaning to the term annual value. Hence, the term annual value is to be construed in common parlance.

'Annual value' refers. to the inherent capacity of a property to earn income or the amount for which the property may reasonably be expected to be let out from year to year.

Thus, it is not the receipt of the actual rent but the capacity of the property to fetch rent which is determinant of its annual value. This implies that a property need not necessarily be let out. Annual value of a property depends the use of the property-self occupied, let out or partly vacant etc.

The provisions of section 23 for determination of annual value are given below:

5.2 Determination of Gross Annual Value [GAV]

As per section 23(1)(a), Annual value of a property is higher of the two viz.:-

- (i) actual rent (AR), or
- (ii) reasonable lettable value (RLV).

(i) **Actual rent [AR]** means the rent received or receivable if the property is actually let out by the owner ; and

(ii) **Reasonable lettable value [RLV]** means the expected rent, which the property might reasonably be expected to yield from year to year. It is not necessary that a property must be let out. Where a property is not let out, RLV may be estimated based on the following factors.:

- (a) Fair rent or the rent of similar properties in the same locality. The fair rent may be different in different circumstances or different contractual obligations.
- (b) Municipal ratable value is the value of the property fixed by the local authorities for the purposes of assessment of local taxes payable. It is normally based on the market rent receivable in respect of a property and is therefore considered as a reliable yardstick to determine the reasonable letting value of the property.
- (c) Standard Rent is the rent fixed under the Rent Control Act to control or limit the prevailing rents in a locality. The landlord cannot charge more rent than the limit fixed under the law. However, the landlord is free to charge lower rent than the rent fixed under the law. Thus, actual rent can be more or less than the fair rent but can never exceed the standard rent.

The following diagram depicts the legal position:

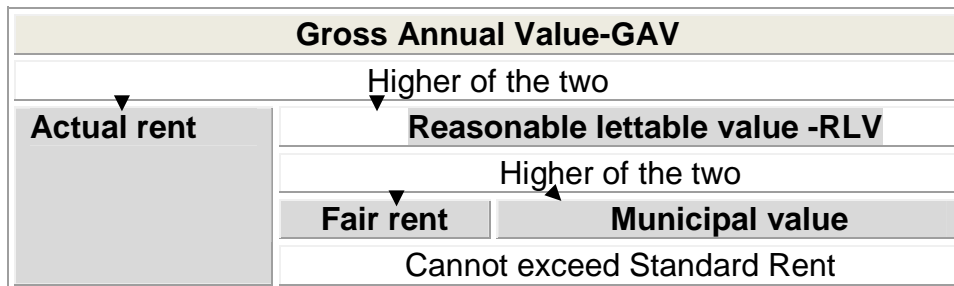


Illustration-1:

Find out the Gross Annual Value from the details given in respect of premises:

Actual Rent: Rs. 10,000 per month.

Rent of similar premises in the area, Rs.. 15,000 per month.

Municipal ratable value, Rs.. 8000 per month

Standard Rent fixed under the Rent Control Act. Rs.. 12,000 p.m.

Solution:

	Rs.	Rs.
Actual rent :Rs. 10,000 p.m.		1,20,000
(a) Fair rent: Rs. 15,000 p.m.	1,80,000	
(b) Municipal ratable value @ Rs. 8,000 p.m.	96,000	
Higher of the (a) and (b) – fair rent	1,80,000	
Standard Rent Rs. 12,000 p.m.	1,44,000	
Fair rent cannot exceed the Standard Rent. Reasonable lettable value RLV restricted to:		1,44,000
Gross Annual Value Higher of two		1,44,000

Illustration-2:

What will be the GAV if the Standard rent Rs.. 18,000 p.m.?

Solution:

	Rs.	Rs.
Given Actual Rent: Rs. 10,000 p.m.		1,20,000
(a) Fair rent - Rs. 15,000 p.m.	1,80,000	
(b) Municipal ratable value: Rs. 8000 p.m.	96,000	
Higher of the (a) and (b) – Fair Rent	1,80,000	
Standard Rent Rs. 18,000 p.m.	2,16,000	
Reasonable Lettable Value RLV		1,80,000
Gross Annual Value Higher of the Two		1,80,000
<i>Standard rent being only a limiting factor is ignored.</i>		

Illustration-3:

What will be the annual value of the property if the Actual rent in the above case is Rs. 20,000 per month; fair rent, ratable value and standard rent remain at the same level of Rs.. 15,000, 8000 and 12,000 per month respectively.

Solution:	Rs.	Rs..
Given Actual Rent -Rs. 20,000 per month		2,40,000
(a) Fair rent - Rs. 15,000 per month	1,80,000	
(b) Municipal ratable value@8000 p.m.	96,000	
Higher of the (a) and (b) – Fair Rent	1,80,000	
Standard Rent Rs. 12,000 per month	1,44,000	
Fair rent cannot exceed the Standard Rent		1,44,000
Reasonable Lettable Value RLV restricted to		
Gross Annual Value (Higher of two)		2,40,000

5.2.1. Comparison of RLV and AR - Section 23(1(b)) :

Gross annual value is the higher of the two values, namely the rent received or receivable as compared with the reasonable letting value. Such comparison may throw two possibilities viz:-

- (a) Actual rent received/ receivable is more than the reasonable letting value. In such a case, actual rent will be the Gross Annual Value u/s 23(1) (b). OR
- (b) Conversely, the reasonable letting value is more than the actual rent received/ receivable. In this case if the reason for deficiency or shortfall between the actual rent the reasonable letting value is :
 - I. Vacancy only and no other reason, such lower rent will be taken as the gross annual value u/s 23(1)(c) or and
 - II. Any other reason, reasonable letting value will be the gross annual value.

The above position is shown in the following diagram:

<u>Situation</u>	<u>Gross Annual Value</u>	
Actual Rent > RLV	Actual Rent	
RLV > Actual Rent	Reason Vacancy	Actual Rent = GAV
	Other reason	RLV = GAV

5.3. Other Important points:-

- (i) Actual rent is relevant only if the property is let out. For a property, which remains vacant or is not let out at all or a self-occupied property cannot have any actual rent, reasonable letting value alone will be the guiding factor.
- (ii) The amount of Rent actually received/ receivable during the previous year will be arrived after deducting rent for the

period for which the property was vacant and unrealised rent or bad debts,

- (iii) In case of composite rent, expenses on providing amenities to the tenant such as water will be deducted to find out the actual rent.
- (iv) For determining the Annual value, the actual rent shall not include the rent, which cannot be realised by the owner. However, the following conditions need to be satisfied for this:
 - (a) The tenancy is bona fide;
 - (b) The defaulting tenant has vacated, or steps have been taken to compel him to vacate the property.
 - (c) The defaulting tenant is not in occupation of any other property of the assessee;
 - (d) The assessee has taken all reasonable steps to institute legal proceedings for the recovery of the unpaid rent or satisfied the Assessing Officer that legal proceedings would be useless.

Illustration-4

Find out the annual value of a house let out for @ Rs. 2,000 per month. Reasonable Lettable Value is Rs. 20,000.

Solution:

Annual value will be the actual rent of Rs. 24,000 because it is higher than the reasonable lettable value of Rs. 20,000

Illustration-5

What will be the GAV if the reasonable lettable value is Rs. 30,000 but the actual rent is Rs. 2,000 per month?

Solution:

Annual value will be the reasonable lettable value i.e. Rs. 30,000 being higher than the actual rent of Rs. 24,000,

Illustration-6

A house was let out on a monthly rent of Rs. 20,000 for 8 months only. Remaining 4 months it remained vacant. Reasonable lettable value of the house is Rs. 2,40,000. What would be its annual value?

Solution:

Actual rent is Rs. 1,60,000 for 8 months . However, RLV is Rs. 2,40,000 for the full year. There is a shortfall of Rs. 80,000 compared to the reasonable lettable value.

Actual rent for full year will Rs. 2,40,000, if there is no vacancy Since the shortfall of Rs. 80,000 is solely on account of vacancy, the gross annual value will be Rs. 1,60,000 being the actual rent.

5.4. Computation of net annual value:

Section 23 classifies the house properties into different categories as discussed below:

(i) Self-occupied business properties:

Income from house property used for own business or profession is exempt from tax. If any rent or other income is generated from such property, the same should be treated as business income. Similarly, municipal taxes, repairs., insurance premium, and other expenses incurred on such property etc. will be admissible as business expenses.

(ii) Self-occupied Residential Properties (SOP):

Following are the provisions in respect of the annual value of a self-occupied residential property.

A. Annual value to be taken as NIL

Under Section 23(2) annual value of a house or part of a house which is in the occupation of the owner (self-occupied property) for the purposes of his own residence shall be taken to be nil.

The exemption will be available in respect of a property which cannot actually be occupied by the owner by reason of the fact that owing to his employment, business or profession carried on at any other place and he has to reside at that other place in a building not belonging to him

B. Exceptions- Section 23(3)

The exemption will not be available in following two cases:-

- a) If the house or part of the house is actually let during the whole or any part of the previous year; or
- b) any other benefit therefrom is derived by the owner.

C. More than one properties – Section 23(4)

Where the self-occupied property consists of more than one house, then the exemption shall be available only in respect of one of such houses, which the assessee may, at his option, specify in this behalf.

The annual value of the other house or houses shall be determined if such house or houses had been let out.

In other words, where the assessee *owns more than one* self-occupied *properties*, the assessee, at his option, may *choose any one* property as self-occupied by him.

The remaining properties will be deemed or assumed to have been let-out (DLP) even if they are occupied by him and not actually let out. Annual Value of such properties deemed to have been let-out will be determined based on their notional

rental value as if the properties were let-out even if no rent has actually been received by the assessee. Deductions u/s 23 & 24 will be allowed in the normal manner on such property.

D. Exemption only to individuals and HUFs:

This exemption is available only to *individuals and HUFs*. Other non- living persons cannot avail this exemption.

E. No Deductions allowed from SOP except Interest:

Where the annual value of a SOP is taken as nil, no deduction will be allowed from such annual value u/s 23 or 24 except in respect of interest paid or payable on borrowed funds. In other words, municipal taxes will not be allowed as deduction while computing, nor repair allowance of 30% of annual value will be allowed u/s 24.

F. Provisions regarding deduction of interest : -

Following is the gist of provisions in respect of deduction of interest on borrowed capital from income from house property:-

Amount of deduction

Deduction in respect of the amount of any interest payable on capital where the property has been acquired, constructed, repaired, renewed or reconstructed with borrowed capital will be allowable. The amount of deduction will be restricted to actual amount subject to following limits:-

- a) Rs. 30,000 if the amount was borrowed prior to 01-04-1999 to acquire, construct renew or restructure the property.
- b) Rs. 30,000 if the amount is borrowed after 01-04-1999 for repairs of the house property
- c) Rs. 2,00,000 if the amount was borrowed after 01-04-1999 to borrowed
 - (i) to acquire or construct the property and
 - (ii) such acquisition or construction of the property is completed within 3 years. from the end of the financial year in which capital was borrowed,

(i) Pre-construction interest

Interest payable on capital borrowed to acquire or construct the house property, for the period prior to the previous year in which the property has been acquired or constructed, will be allowed as deduction in five equal instalments beginning from that previous year and for each of the four immediately succeeding previous years.:

(ii) Interest allowed under other provisions :

Amount of interest will be reduced to the extent it is allowed under any other provision of the Act.

(iii) Interest on new loan to pay old loan :

Where the assessee, subsequent to the capital borrowed for construction or acquisition etc. of property takes a new loan to make repayment of old loan, interest payable on such new loan will also be allowed. However, any interest payable on interest will not be allowed as deception.

(iv) Accrual basis

Interest on capital borrowed is allowed as deduction when it is accrued. Actual payment during the previous year is not necessary.

(v) Other provisions:

(vi) Brokerage or commission paid to arrange a loan for house construction is not allowed as deduction.

(vii) Interest payable on loan taken for construction etc. of a property is allowed and not on any loan taken for payment of interest.

(viii) Any loss arising under the head 'income from house property' may be set-off against the other heads in the same assessment year for a period of 8 years. from the year of loss.

(ix) The assessee is required to furnish a certificate, from the person to whom any interest is payable on the capital borrowed, specifying the amount of interest payable by the assessee for the purpose of such acquisition or construction of the property, or, conversion of the whole or any part of the capital borrowed which remains to be repaid as a new loan.

INTEREST ALLOWABLE ON LOANS TAKEN		
Before 01/04/1999	ON OR AFTER 01/04/1999	
Rs. 30,000	For Acquisition Construction	or For Renovation or Repairs.
	Rs. 2,00,000	Rs. 30,000

Illustrations-7:

Find out the interest deductible U/s 24 for A.Y. 2018-19, if A borrows Rs.. 25,00,000 @ 6% p.a. on 1/4/2013 to construct a Bungalow for own residence completed in May ,2017.

Solution:

The Bungalow is constructed within three years. of taking the loan, Rs..1,50,000 will be allowed out of interest payable Rs.. 2,50,000. Interest paid in F.Y2013-14, 2014-15 & 2015-16 Rs. 4,50,000 will be allowable in five equal instalments of Rs. 90,000

for five years. beginning from A.Y. 2018-19. Total deduction, will be limited to Rs. 2,00,000.

Illustration-8:

Determine the amount of interest allowable in the above illustration if the money was borrowed in 1998.

Solution

The deduction would be restricted to Rs.. 30.000.

Illustration-9:

What would be amount of deductible interest if the loan was used for repairs. of the bungalow?

Solution

The deduction would be restricted to Rs.. 30.000.

Illustration-10:

If the construction of the Bungalow was completed in June 2015, what would be the amount of deductible interest?

Solution:

The construction is not completed within three years. of taking loan; the deduction will be restricted to Rs. 30,000.

5.5. Let-out Properties (LOP)

Following principles will be applicable for determination of annual value of properties let out including deemed to be let out. (Self-occupied properties (DLP))

5.5.1 Net Annual Value (NAV)

Net annual value of a let-out property value (NAV) is arrived at by deducting Municipal taxes *paid* by the owner from GAV- (Proviso to S. 23(1). Municipal taxes paid or borne by the tenant are not deductible. Municipal taxes are taken on cash basis and not accrual basis.

$\text{NAV} = [\text{GAV}] - [\text{Municipal Taxes paid by the Owner}]$
--

5.5.2 Deductions under section 24:

a) Standard deduction

From the net annual value (NAV), a standard deduction in respect of repairs. and collection charges is allowed to the extent of 30% of the net annual value irrespective of whether the assessee has actually incurred the expenses or not. However, if the repairs. are borne by the tenant, this deduction will not be allowed in the hands of the owner of the property.

(b) Interest on funds borrowed

Interest on loan taken for acquisition, construction, renewal, repairs or reconstruction is allowed on let-out properties without limit of Rs. 30,000/ 2,00,000 unlike in case of a SOP. The interest on loans is allowable on accrual basis. Similarly, pre-construction interest from the date of the loan to the end of the previous year before the previous year in which

the house was acquired is amortized 1/5th per year for 5 years. as in case of SOP from the financial year in which the construction was completed.

Illustration -11

A took a loan on 01/10/ 2010 of Rs. 10,00,000 @ 10% interest p.a for the construction of his house. The house was finally constructed on March 31, 2013. Calculate the pre-construction period interest and also mention the assessment years., in which the deduction for such interest may be allowed.

Solution

- Loan was taken on 01/10/2010
- the house constructed in F.Y. 2012-13 (A.Y. 2013-14)
- Interest for preconstruction period 01/10/2010 to 31/03/2013 2-1/2 years. X Rs. 10,00,000 X 10% = Rs. 2,50,000.
- Interest to be amortized in five equal instalments of Rs. 50,000 each from A.Y 2013-14 till 2018-19.

6. Property let-out and self-occupied for part of the year

A property is let-out for whole or any part of the year and self-occupied for the remaining part of the year, shall be treated as let-out property and computation will be made accordingly by comparing actual rent with the fair rent for the whole property u/s 23(1). It will not be treated as SOP as Section 23(3) makes it clear the SOP shall not be let-out for any part of the year nor should any benefit be derived from it.

7. Property partly let-out and partly self-occupied:

If a part of the property – say one or two floors or few rooms have been let out and another part of the property is self-occupied, then for each portion the calculation will be made separately. Relevant expenses like property taxes and interest will be allocated suitably for each portion and deductions will be allowed separately for each portion.

Note the difference between properties let out /SOP for split period and with split portion used for letting out/SOP.

8. Co-ownership – Section 26:

A property owned by more than one owners having definite and ascertainable share therein, will not be assessed as an association of persons but share of each owner shall be included in his individual income. Supposing the co-owners. themselves occupy the property, share of each owner will be treated as nil. Each of the co-owners. would be entitled to the deduction in respect of interest subject to the limit of Rs. 30,000 or Rs. 1,50,000, as the case may be.

6. MISCELLANEOUS:

A. Recovery or realization of past arrears / unrealised rent.

As per the section 25A, which has been introduced in place of the old sections 25A, 25AA and 25B, arrears. of rent or

any unrealised rent will be taxable in the year when it is realised or recovered regardless of whether the assessee does or does not own the property in the that year and 30% deduction is allowable in that year.

B. TDS

Interest paid to a non-resident outside India without deduction of tax at source will not be allowed as deduction.

C. Set off and carry forward of losses :

Any loss arising under the head "Income from House Property" in respect of interest only can be set off against income arising from other heads and the remaining loss will be allowed to be set off and carried forward for a period of 8 assessment years.

D. No other Deductions allowed;

No deduction would be available in respect of charges like electricity, land revenue, ground rent, insurance, etc. even though they may be actual outgoings since the standard deduction of 30% is supposed to take care of all expenses.

7. ILLUSTRATIONS:

Illustration-12

Find out the Gross Annual Value in the following cases:-

Particulars.	Property				
	i.I	ii.II	iii.III	iv.IV	v.VV
Municipal Value	5000	5000	5000	5000	5000
Rent Received	5200	5200	5700	5700	6000
Fair Rental Value	5600	5600	5600	5800	6100
Standard Rent under [Rent Control Act]	NA	5500	5500	5500	7300

Solution:					
	I	II	III	IV	V
Municipal Value	5000	5000	5000	5000	5000
Rent Received	5200	5200	5700	5700	6000
Fair Rental Value	5600	5600	5600	5800	6100
Standard Rent under Rent Act	NA	5500	5500	5500	7300
Gross Annual Value	vii.5600	viii.5500	ix.5700	x.5700*	xi.6100*

- House I- Fair Rent being highest
- House II- fair rent Rs. 5,600 limited to Standard Rent Rs. 5,500
- House III : Actual Rent being higher Rs. 5700
- House IV Actual rent Rs. 5,700 being higher than RLV i.e. Fair Rent Rs. 5800 limited to Standard rent Rs. 5,500

- House V – Fair rent being the highest Rs. 6100. Standard rent is only a limiting factor, hence ignored.

Illustration-13

A owns two houses, I & II. House I is let-out throughout the previous year. House II is self-occupied for nine months and let-out for three months on a monthly rent of Rs. 5,000. Determine Taxable income, given the following details:-

	xiii. House I	xiv. House II
Municipal Value	40,000	50,000
Fair Rent	50,000	48,000
Rent Received	48,000	15,000
Municipal Taxes paid	4,000	5,000
Insurance Premium (not yet paid)	2,000	2,500
Ground Rent	1,000	1,500
Maintenance Charges	3,000	3,500
Electricity Bill	5,000	6,000

Solution:

	xvi. House I	xvii. House II
Gross Rental Value (fair rent for house I and municipal value for house –II)	50,000	50,000
Less : Municipal Taxes paid	4,000	5,000
Net Rental Value	46,000	45,000
Less : Deduction u/s 24		
Repairs & Collection Charges 30%	13,800	13,500
Taxable Income	32,200	31,500

8. SELF EXAMINATION QUESTIONS:

1. What is annual value? How is it determined?
2. Discuss briefly the various expenses and allowances that are deductible under the head "Income from House Property"
3. Mention the amounts which are not deductible from Income from House Property
4. Write a short note on property owned by co-owners.
5. Explain briefly (a) Owner of a house property (b) A member of a co-operative society (c) Annual Value
6. What do you mean by "Self-Occupied house property"? How is the annual value of such property determined?
7. Explain briefly, house property "deemed to be let-out" and how the income from such house property is determined?
8. Is interest paid on a housing loan out of India allowable as a deduction?

9. Explain with reason if the Interest paid by the assessee on borrowed capital in the construction of the property, till the date of letting out an admissible expenditure.
10. Discuss the provisions of Income Tax Act regarding unoccupied residential house?
11. Enumerate and explain if any, the exceptions to the rule that Ownership is the criterion for assessment of Income from house property under Section 22"
12. Discuss tax liability of arrears. of rent.
13. Explain the provisions of the Income Tax Act with respect to the computation of income from a self-occupied house property.
14. Explain the tax treatment of unrealized rent.
15. Lakdawala completed construction of a residential house on 1.4.1999. Interest paid on loans borrowed for construction during the 2 year prior to completion was Rs. 20,000/- and for the current years was Rs. 10,000 The house was let out on a monthly rent of Rs.. 4,000/-. Annual Municipal tax was Rs. 6,000/-. Interest paid during the year is Rs.. 15,000/-. Amount spent on repairs. is Rs.. 2,000/-. Fire insurance premium paid is Rs. 1,500/- p.a. The property was vacant for 3 months. Annual letting value is Rs.. 30,000/-. Compute the "Income from House Property" for AY 2018-19 (*Ans. Rs.. 8,500*)
16. Ram owned a house property at Chennai which was occupied by him for the purpose of his residence. He was transferred to Mumbai in June 2017 and therefore he let-out the property with effect from July 1, 2017 on a monthly rent of Rs.. 3,000/-. The municipal tax payable in respect of the property was Rs.. 6,000/- of which only 50% was paid by him before 31.3.2018. Interest on money borrowed for the construction of the property amounted to Rs.. 20,000/- Compute the income from house property for the AY 2012-13(*Ans. Loss Rs. 8250*)
17. Arvind commenced his construction of a residential house intended exclusively for his residence on 1.11.2012. He raised a loan of Rs.. 5,00,000/- at 10% interest for the purpose of construction on 1.11.2006. Finding that there was an overrun in the cost of construction he raised a further loan of Rs..8 lakh at the same rate of interest on 1.10.2014. What is the interest allowable under Section 24 assuming that the construction was completed on 31.3.2016?
(*Ans. Loss Rs.. 1,50,000 pre- construction interest 1/5th*)
18. From the following particulars of his property furnished by S, compute income from house property . S owns a residential house actually let out for 10 months for total rent of Rs.. 25,000. Fair rent of this house is Rs.. 27,000 and municipal ratable valuation is Rs.. 24,000. Total outgo on

account of this house included repairs. of Rs.. 9,000, Municipal taxes of 18 months Rs.. 9,000 and insurance premium of Rs.. 1,500. Interest on funds borrowed amounted to Rs.. 1,75,000.

He also owns another residential house at Andheri, which is used for own residence. Fair rent of this house is Rs.. 80,000 and municipal ratable valuation is Rs.. 75,000. Total outgo on account of this house included repairs. of Rs.. 6,000, Municipal taxes Rs.. 18,000 and insurance premium of Rs.. 1,500. Construction of this house was complete in 2016 from the funds borrowed from HDFC. During the current year, interest amounting to Rs.. 90,000 was paid for the current year and Rs.. 60,000 for the last year. A further interest of Rs.. 65,000 was paid on loans taken for renovation necessitated due to heave rains. The interest pertains equally to this year as well as the last year. ((Ans: L.O.P - loss 1,63,000 , SOP 1,50,000 –interest paid)

19. State with reason whether the following incomes will be taxable as income from house property.
- R lets out his house to Y for using it as his office.
 - R uses his house as the godown to store his factory goods.
 - R rents out his property as residential quarters to the workers in his factory at a nominal rent of Rs..500 p.m.
 - R enters into a written agreement to purchase a property from Y for Rs.. 5,00,000 . He has paid the consideration and taken the possession of the property but the property is yet to be registered in the name of R.
 - R owns a property, which is given on lease to Y for a period of 6 years, lease rent being Rs..10,000 per month. Y has a right to get the lease renewed for a further period of 6 years.
 - R owns a property, which is given on lease to Y for a period of one month, Y has a right to get the lease renewed for a period of one month, in each subsequent month, and such renewal is possible with mutual consent till 2020.
 - R owns a property, which is given on rent to Y. Y annually pays Rs..1,50,000 as rent of the building as well as the charges for different services ;lift, security, etc. provided by R.
 - R owns an air-conditioned furnished lecture hall. It is let out, annual rent being Rs. 5,00,000, which includes rent of building as well as rent of air conditioner and furniture.
(Ans : a, d, e, f, and g]



PROFITS AND GAINS OF BUSINESS OR PROFESSION (Sections 28 to 44)

SYNOPSIS:

1. Introduction and objective
2. Concept of business & Profession
3. Scheme of computation
4. Deductions expressly allowed under the Act
5. General deductions
6. Specific disallowances
7. Chargeability of profits -Section 41
8. Miscellaneous provisions
9. Presumptive income
10. Typical Illustrations
11. Self-Assessment Questions

1. INTRODUCTION AND OBJECTIVE

The income under the head “profits and gains of business and profession” includes “profits” and “gains” of “Business” and “Profession” including their different types and forms viz. vocation, trade, commerce, manufacture and any adventure in the nature of trade or profession.

The lesson covers various aspects of the income from the head “Profits and gains of business and profession”, its computation, general and specific deductions allowable under this head and also items not allowed as deduction to the extent contained in Sections 28 to 32, 35, 36, 37, 40, 40A, 43B

2. CONCEPT OF BUSINESS AND PROFESSION :

2.1 Definitions

2.1.1. Business :

Sec. 2 (13) defines Business as under - :

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

The definition of “business” is an inclusive one. It includes “business” in its general commercial sense but also several other activities, namely- trade, commerce, manufacture and any adventure in the nature of trade, commerce or manufacture.

Business, trade and commerce refer to buying and selling of goods or services for profit and other incidental activities. Manufacturing means producing new goods or articles.

2.1.2. Profession

Section 2(36) gives an inclusive definition of “profession” viz. **“Profession” includes vocation**”.

“Profession” in common parlance means rendering of skilled services like as those of doctors, architects, lawyers, chartered accountants or other professionals.

Vocation means a specified occupation, profession or trade or calling or career especially a religious one. It will therefore include services of priests, preachers delivering sermons or discourses, management gurus, yoga gurus, palmists and astrologers, tarot readers, plumbers, mechanics, priests performing havan or pooja etc.

2.1.3. Adventure

The phrase “Adventure in the nature of trade, commerce or manufacture” indicates that business or profession need not be organised, systematic or regular. A single act may constitute a business or profession. For instance, when a land was purchased, developed and subdivided in smaller plots for resale was held as an adventure in the nature of trade or commerce or manufacture.

2.1.4. Provisions to apply uniformly

Income under this head will be uniformly chargeable to tax regardless of the following considerations:-

- a) **Type or description** of an activity namely a business, a profession, or an adventure in the nature of business or profession. However, there are some provisions dealing with some specific cases such as presumptive tax applicable to different activities.
- b) **Legality or illegality** of the activity. Accordingly, income from theft, bribery or smuggling or other criminal or illegal activities will be chargeable to tax under this head just like the income of a legal and legitimate business or profession.
- c) **Regularity or irregularity** of the business or profession. A business or a profession may be regular, irregular or occasional. Even the activity of a single activity or adventure will be chargeable under this head if it is in the nature of a business or a profession.
- d) **Organised or unorganised** ; and
- e) Whether or not requires **personal talents or skill**.

3. SCHEME OF COMPUTATION -SEC. 28-29

3.1. Chargeable income- (Sec 28) :

Under Sec 28, following income are chargeable to income-tax under the head "Profits and gains of business or profession",—

(i) the profits and gains of any business or profession, which was carried on by the assessee at any time during the previous year;

Compensation for termination or modification of contracts

(ii) any compensation or other payment due to or received by any person at or in connection with the termination of contract modification of the terms and conditions relating thereto for ;

- a. managing the whole or substantially the whole of the affairs of an Indian company;
- b. managing the whole or substantially the whole of the affairs in India of any other company;
- c. holding an agency in India for any part of the activities relating to the business of any other person by any person;
- d. vesting in the Government, or in any corporation owned or controlled by the Government, under any law, 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;

Export incentives

(iiia) profits on sale of an import licence ;

(iiib) cash assistance received or receivable by any person against exports under any scheme of the Government of India ;

(iiic) duty drawback in respect of customs or excise duty person against exports ;

(iiid) any profit on the transfer of the Duty Entitlement Pass Book Scheme (DEPB);

(iiie) any profit on the transfer of the Duty Free Replenishment Certificate;

(iv) 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 due to or received by a partner of a firm as adjusted by any amount not allowed to be deducted u/s 40(b);

Non- compete agreement

(va) any sum, whether received or receivable, in cash or kind, under an agreement for not carrying out any activity in relation to any business or profession or not sharing any know-how, patent, 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 if such amount is -

- chargeable under the head "Capital gains"; or
- received as compensation, from the multi-lateral fund of the Montreal Protocol on Substances that Deplete the Ozone layer under the United Nations Environment Programme(UNEP), in accordance with the terms of agreement entered into with the Government of India.

(vi) any sum received under a Keyman insurance policy including the sum allocated by way of bonus on such policy;

(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 (scientific research) in earlier years;

(viii) Amount recovered on account of bad debts allowed in the earlier years;

(ix) Speculation Business

Speculation business is deemed to be distinct and separate from any other business if speculative transactions; which are settled by payment of difference in price of goods or securities and not by actual delivery; carried on by an assessee are of such a nature as to constitute a business.

3.2. Computation of business income –Section-29:

As per section 29, income under the head profits and gains of business or profession shall be computed in as per the provisions of sections 30 to 43D. On a collective the provisions of the two sections, following points emerge out:

1. Income under this head is the aggregate of all income:
 - (i) from different sources specified in Sec 28 ;
 - (ii) in respect of a business or profession ;
 - (iii) carried on by the assessee.

(iv) any time during the previous year ;

2. From the aggregate income, deduction will be allowed in respect of expenses

- (i) incurred by the assessee ;
- (ii) during the previous year ;
- (iii) for earning such income .

3. The deduction of expenses incurred is subject to the following principles or conditions:-

- (i) Expenses will not be deducted, if the business or profession is closed down during the previous year.
- (ii) Expenses incurred before setting of the business will not be allowed except where specifically provided by law.
- (iii) Some expenses are fully deductible, while others are deductible only partially ;
- (iv) Similarly, some deductions are assessee -specific i.e. allowable to some classes of assessees e.g. a company or a firm but not to others ;
- (v) Some deductions are without conditions, while others are subject to fulfillment of conditions attached with the deduction.

3.3. Basic Scheme of computation –Sec 28- 43D

From the above, scheme for computation of income under the head profits and gains of business and profession may be summarised as under:-

- (a) Sec. 28 is the charging section. It defines what constitutes income under the head profits and gains of business or profession.
- (b) Sec. 29 provides mode of computation of taxable income under this head viz. by deducting expenses from income.
- (c) Sec. 30 to 35 provide expressly for deduction of expenses in some cases
- (d) Sec 36 and 37 provide for general deductions.
- (e) Sec. 40, 40A and 43B provide for non- deduction in certain circumstances; of expenses, which are otherwise deductible.
- (f) Section 44A to 44D provide for computation of income on presumptive basis in case of smaller assesseees like , insurance agents retailers, construction contractors, transporters etc.

3.4. Method of Accounting: (Sec 145 / 145A)

3.4.1 As per section 145(1), income chargeable under the head “Profits gains of business or profession “or” income from other sources may be computed according to either cash or mercantile system of accounting regularly employed by the assessee.

a) Mercantile system or accrual system of accounting

Under the mercantile or accrual system of accounting, income and expenditure accrued during the previous year will be recorded in the books and the taxable income from profits or gains from such a business or profession will be the difference between the expenses or income accrued during that previous year.

Actual receipt of the income or payment of expenses during the year is not mandatory. Instead, such income may be received, or expenses may be paid in the previous year or in a year preceding or following the previous year.

b) Cash system of accounting

Under the cash system of accounting, incomes actually received, and expenses actually paid during a particular previous year will be recorded and considered for computing taxable profits or gains from a business or a profession. Net profit under the cash system will be equal to the difference of incomes received and expenses paid during the accounting year whether such receipts and payments relate to that particular year or some other year or years.

c) Hybrid system of accounting

When accounts are maintained as per the accrual or mercantile system, but some items of income or expenses on cash or receipt basis, it is called hybrid system of accounting because it combines the features of both the methods. Even statutorily, section 43B provides for deduction of specified statutory dues only when they are actually paid although the method of accounting employed may be mercantile.

Illustration-1:

A earns commission in the financial year 2017-18 but receives it in the year 2018-19. Under the mercantile system, the commission will be taxed in the year of earning it viz 2017-18 or A.Y. 2018-19, although not actually received during that year.

Under the cash system, it would be taxed in the year of actual receipt P.Y. 2018-19 (A. Y. 2019-20), although not earned in that year.

3.4.2 Income Computation & Disclosure Standards

As per Sec 145(2), the Central Government may notify in the official gazette from time to time Accounting Standards to be followed by any class of assessee or in respect of any class of income. Such accounting standards are called *Income Computation and Disclosure Standards (ICDS)*. So far, the CBDT has notified 10 *Income Computation and Disclosure Standards (ICDS)*, effective from A.Y. 2017-18 onwards.

4. DEDUCTIONS EXPRESSLY ALLOWED

The following expenses are expressly allowed as deductions against profits and gains of business or profession:

4.1 Rent, Rates, Taxes, Repairs & Insurance for Building-Section 30

Vide section 30, rent, rates, taxes, repairs and insurance for premises, used for the purposes of the business or profession are deductible as under:-

- a) The amount paid as **rent** or on account of **repairs** of in respect of the premises occupied by the assessee as tenant .
- b) the amount paid on account of current repairs to the premises occupied by the assessee otherwise than as a tenant,
- c) any sums paid on account of land revenue, local rates or municipal taxes subject to the provisions of section 43B ; and
- d) the amount of insurance premium paid against risk of damage or destruction of the premises .

The deduction is subject to the following modifications:-

- (i) Capital expenses are not allowed as deduction under this section.
- (ii) Where a part of any premises is partly used as dwelling house by the assessee, the deduction will be restricted to proportionate amount of rent or repairs determined by the assessing office applicable the part of the premises used for business/ profession- section 38.

4.2 Repairs & Insurance of Machinery, Plant & Furniture-Section 31:

Under Sec. 31, the following deductions are allowed in respect of repairs and insurance of machinery, plant or furniture used for the purposes of the business or profession:—

- (i) the amount paid on account of current repairs thereto if such expenses are revenue expense and not capital expenses;

(ii) the amount of any insurance premium paid against risk of damage or destruction thereof.

In a case, where the building, machinery, plant or furniture is not exclusively used for the purposes of the business or profession, the deduction shall be restricted to a fair proportionate part thereof which the assessing officer may determine, having regard to the user of such building, machinery, plant or furniture for the purposes of the business or profession.

Machinery hire charges are allowed not u/s 31 but u/s 37 as residual expenses.

4.3. Depreciation - Section-32:

4.3.1 *Conditions for claiming depreciation:*

U/s 32 an assessee is entitled to claim deduction in respect of depreciation in computing the total income if he fulfills the following conditions:-

(i) *Claim not necessary*

Depreciation will be allowed as deduction irrespective of whether or not the assessee has made a claim for deduction so long as the conditions for the allowance of depreciation are satisfied.

(ii) *Depreciation allowed on eligible assets only:*

Depreciation will be allowed only on the following assets called depreciable assets.

a) *Tangible assets;*

buildings, machinery, plant or furniture,

b) *Intangible assets*

Know-how, patents, copyrights, trademarks, licences, franchises or any other business or commercial rights of similar nature.

“Building” means only the superstructure, not the land on which it is constructed.

“Plant” includes ships; vehicle, books including technical know-how; scientific apparatus and surgical equipment used for the purpose of business or profession but does not include tea bushes or livestock or buildings or furniture and fittings.

(iii) *Assets not eligible for depreciation*

Following assets are not eligible for depreciation:

- a) Foreign car - acquired between 01/03/ 1975 and 31/03/ 2001 (only academic as *foreign cars purchased on or after 01/04/2001 will be eligible for depreciation* ; and
- b) Any machinery or plant if the actual cost thereof is allowed as a deduction in one or more years under an agreement entered into by the Central Government under Section 42.

(iv) *Ownership – Partial ownership:*

Assessee must own the depreciable asset wholly or partly as the sole owner or the co-owner thereof. In case of an asset owned by different assessees, each co-owner will be entitled to depreciation on his contribution to the cost of asset.

Exception:

Depreciation will be allowed on capital work or renovation or construction of any structure in building though *not owned* by the assessee, which is held on lease or other right of occupancy and the new structure is owned by the assessee

(v) *Purpose or user of the assets*

The assessee must use the asset for the purpose of his business or profession.

(vi) *User of the assets during the previous year:*

An asset acquired by the assessee during the previous year should be put to use for the purposes of his business or profession for a period of 180 days or more. In such a case, the assessee will entitled to claim deprecation at full rate prescribed.

If the asset is put to use during the previous year for a period of less than 180 days; i.e. 179 days or less; depreciation will be allowed @ 50% of the rate prescribed.

The condition is applicable on an asset *acquired during the year* and no other asset. This is because the machinery would undergo wear and tear even if it was not put to actual use

Illustration -2

A Machine is purchased on 31/03/2017, is put to use on 01/04/ 2017.

No depreciation will be allowed depreciation in A.Y. 2017-18 because the machine though acquired, is not put to use during the previous year 2016-17. Full depreciation will be allowable A.Y. 2018-19.

4.3.2 Additional Depreciation- Section 32(1)(ia)

U/s 32(1)(ia), (read with Sec 32AD) provides for allowing additional depreciation over and above the *normal depreciation as per the following scheme:-*

(i) Eligibility assessee

Any assessee being an *industrial undertaking* engaged in the business of *manufacture or production of any article or thing, or transmission of power.*

(ii) Rate of additional depreciation allowable

- a) 20% of the actual cost of new plant or machinery (not being ships or aircrafts) acquired and installed after 31st March, 2005.
- b) 35% of the actual cost *in case of the assessee being a* manufacturing undertaking or enterprise set up in the notified backward areas of the States of Andhra Pradesh, Bihar, Telangana and West Bengal on or after 1st April, 2015 and the Assessee acquires and installs new plant & machinery between 01-04 2015 & 31-03-2020.
- c) 50% of the above rates i.e. 10% or 17.5%, where the plant or machinery is acquired and installed for less than 180 days of the relevant previous year and the balance 50% will be allowed in the immediately succeeding previous year

(iii) Assets not be eligible for additional depreciation: -

- a. Ships and aircrafts;
- b. Second hand machinery used by any other person in or out of India;
- c. Machinery installed in a residential premises or a guesthouse;
- d. Any office appliances or road transport vehicles;
- e. Any plant or machinery, actual cost of which is already allowed as a deduction e.g. asset for scientific research; and
- f. Buildings, furniture & fittings and old plant.

4.3.3 Important Terms :

(i) Block of Assets

As per Sec 2(11) – “*block of assets*” means a group of assets falling within a class of assets comprising of —

- a) Tangible assets, being buildings, machinery, plant or furniture;
- b) intangible assets, being know-how, patents, copyrights, trademarks, licenses, franchises or any other business or commercial rights of similar nature, in respect of which the same percentage of depreciation is prescribed.

As per the definition, block of assets is a classification of assets based on the twin criteria of:

- (a) Class of asset viz. building, plant, furniture or machinery to which the asset belongs to ; and
- (b) Rate applicable on the asset within that class.

The assets within a class eligible for same rate will form a block of assets but not assets from different groups having same rate nor the assets from different classes having same rate. A block may have a single asset in it.

(ii) Written Down Value (WDV) of an asset

Written down value of an asset means:

- a. actual cost to the assessee of the asset acquired in the previous year, and
- b. the actual cost to the assessee less all depreciation actually allowed thereafter.

(iii) Written Down Value (WDV) of block of assets

Written down value of any block of assets, means

- a. the opening WDV of the block of
 - the assessee or
 - the previous owner or entity, in case of slump sale, amalgamation, succession of business , demerger, conversion into company etc. or holding /subsidiary company)
- b. adjusted by: -
 - (i) *the increase* by the actual cost of any asset falling within that block, acquired during the previous year; and
 - (ii) the *reduction* of the moneys payable in respect of any asset falling within that block, which is sold or discarded or demolished or destroyed during that previous year together with the amount of the scrap value, if any, so however that the amount of such reduction does not exceed the written down value as so increased.

This is depicted in the following chart :

Opening W.D.V. of the block as on 01-04-2017		
ADD		
Actual cost of new assets acquired falling within the block in P.Y. 2017-18		
DEDUCT		
Money received/ receivable / scrap value of the asset falling within the block sold, discarded, demolished or destroyed during P.Y. 2017-18		
RESULT (BALANCE)		
<u>Negative :</u> Taxable as short term capital gain	<u>Zero:</u> No depreciation	<u>Balance but no assets left in block:</u> No depreciation short term capital Loss
Balance of adjusted block with assets		
DEDUCT		
Depreciation at applicable rate		
RESULT		
Closing W.D.V. of the block as on 01-04-2017		

Other important points:

- (i) Any other things or benefit which can be converted in terms of money cannot be deducted
- (ii) If the resultant block value figure is negative because the sale proceeds exceed the original block value plus increases, it will be treated as short term capital gain.

Illustration-3:

Opening value of block having four machines (depreciation @ 25%) is Rs 5,00,000 as at 01/04/2017. On 01/06/2017. Purchased another machine with depreciation @ 25% for Rs 2,00,000. Sold an existing machine for Rs 4,00,000. Ascertain depreciation for the A.Y.2016-17 and the closing value of block as on 31-03-2018.

Solution.

	Rupees
WDV as on 1/4/2017	5,00,000
Add: Purchase during the year	<u>2,00,000</u>
	7,00,000
Less: Sales during the year	<u>4,00,000</u>
Adjusted Block	<u>3,00,000</u>
Depreciation @ 25 per cent	<u>75,000</u>
WDV of block as on 31 /3/2018	<u>2,25,000</u>

(iii) *Actual Cost*

Actual cost is determined on the following principles

- i. *Subsidy or grant to be reduced to determine actual cost*

Actual cost means the actual cost of the assets to the assessee, reduced by that portion of the cost thereof, if any, as has been met directly or indirectly by any other person or authority (subsidy or grant and expenses incurred for acquiring the asset or installation) - Sec.43(1). Grant /subsidy whether of revenue nature or of capital nature are taxable as income, unless it has been reduced from the actual cost of a depreciable asset.

Illustration 4:

ABC purchases a machine for Rs 10 lakh with non-refundable subsidy of Rs. 4 lakh from SIDBI. Actual cost of the machine will be Rs. 6 lakh [Rs. 10 lakh-Rs 4 lakh].

ii. Scientific Research Asset

Actual cost of asset purchased for scientific research and brought into business use will be *Actual Cost minus deduction available u/s 35*.

Illustration 5:

A purchases a machine for scientific research for Rs 10 lakh with the non- refundable subsidy of Rs. 5 lakh from SIDBI. The machine is eligible for deduction u/s 35 to the extent of Rs. 3 lakh. Actual cost of the machine will be Rs. 2 lakh i.e. Rs. 10 lakh- Rs 5 lakh - Rs. 3 lakh

iii. Gift, inheritance etc.

Actual cost of asset acquired by way of *gift* or *inheritance* will be the WDV to the previous owner.

Illustration 6:

If A gifts away to B the machinery in the above illustration, the cost of machine to B will also be Rs. 2 lakh, which was the cost to A.

iv. Enhanced cost

Where in the opinion of the assessing officer, an asset is acquired at an enhanced cost to claim more depreciation and reduce tax liability, actual cost will be equal to the actual cost of asset used and transferred earlier but now reacquired or cost of repurchase, whichever is less.

Illustration 7:

A sold a machinery with WDV of Rs 2 lakh for Rs. 3 lakh and repurchased it after two years at the prevailing market value of Rs. 10 lakh. If the assessing officer is of the opinion that the machine is repurchased for claiming more depreciation, he can ignore the enhanced purchase value of Rs. 10 lakh and treat Rs. 2 lakh as the actual cost.

4.3.4 Mode of computation

Following principles are important in computing the depreciation:

- Depreciation is calculated on the WDV of the block after adjusting the sales and purchase during the year in that block.
- Rates of depreciation for different assets are taken as prescribed in rules.
- Depreciation will not be allowed on a block if-
 - WDV of that block comes to zero, even if some assets in that block may be existing.
 - no assets are left in the block and the become empty, or ceases to exist, . WDV of the block will be treated as short term loss.
- Depreciation will be allowed at 50% of the prescribed rate, if the asset is put to use for less than 180 days in the year of acquisition.
- Straight Line Method (SLM) method is applied in case of the assets of the power companies i.e. undertakings engaged in generation or generation and distribution of power at the prescribed rates of depreciation on the *actual cost* of the assets.
- Additional depreciation of 20% or 35% on actual cost in is allowable as discussed above .
- Different treatment is given to depreciation on foreign cars purchased between 1975- 2001 as depreciation has been denied to such cars subject to some exceptions discussed earlier.
- Depreciation will not be allowed on scientific research assets, entire cost of which is allowed as deduction u/s 35.

4.3.5 Succession of Business

Succession means takeover of a business by another new entity e.g.

- conversion of a firm or sole proprietor to company -section 47(xiii)/(xiv),
- succession of a private or unlisted public company, by limited liability partnership- section 47(xiiib), or
- amalgamation / demerger/ succession of business - section 170.

In such cases, aggregate depreciation for a year will not exceed the amount of depreciation, had such event not taken place and such depreciation shall be apportioned between the old and new entity

Illustration-8

Under a scheme of amalgamation, A Ltd, transfers to B Ltd, machinery having WDV of Rs 3,65,000 on 1/09/2017. Calculate

the depreciation in the hands of A Ltd. & B Ltd. If rate of depreciation is 20%.

Solution:

- Depreciation for the full year if the amalgamation has not taken place : Rs. 73000 [20% on Rs. 3,65,000]
- Aggregate depreciation for A.Y. 2018-19 cannot exceed Rs. 73000
- *Pro rata* allocation of depreciation for the two periods :
 - Pre amalgamation* – $153/365 \times 73000 = \underline{\text{Rs } 30,600}$
[01/04/2017 to 31/08/2017= 153 days]
 - Post amalgamation* – $212/365 \times 73000 = \underline{\text{Rs } 42,400}$
[01/09/2017 to 31/03/2018=212 days]

4.3.6 Depreciation to be allowed even if no claim made

As per explanation 5 to section 32, the depreciation will be allowed whether or not the assessee has claimed the deduction in respect of depreciation in computing his total income

4.3.7 Loss on Sale of Machinery

When an asset is sold, discarded, demolished or destroyed in the previous year following rules apply:

- a) If block has not become empty and the *assets are still existing* in the block and also *some value is left* in the block , sales proceeds/ scrap value will be deducted from the value of the block and depreciation will be allowed on the resultant value of the block after **increase by the actual cost** of assets acquired , if any

Illustration 9:

One of the assets from a block with depreciation @ 30% having WDV of Rs. 5 Lakh is sold for Rs. 1 Lakh; the resultant value of the block will be Rs. 4 Lakh and the depreciation will be Rs. 1.20 Lakh

- b) When the *value of the block comes to zero, but assets still exist* and the block has not become empty, depreciation will not be allowed.

Illustration 10:

A car in a block of four cars with opening WDV of Rs 5 lakhs is sold for Rs. 5 Lakh. The value of the adjusted block will be zero. No depreciation will be allowed although three cars still exist in the block.

- c) If the sale proceeds are more than the adjusted WDV of the block, the resultant surplus will be treated as short term capital gain regardless of the fact that assets are still left in the block or the block is empty.

Illustration 11:

In the above example, the car is sold for Rs 8 Lakh, the resultant surplus of Rs 3 lakh will be taxable as short- term capital gain.

d) If there are no assets in the block and the block becomes empty but the WDV is not fully written off , then

- there will be no depreciation allowance and
- existing WDV will be treated as terminal loss or short term capital loss due to cessation of the block as result of sales,

Illustration 12:

All assets in a block with opening WDV of Rs 5 l sold for Rs 3 Lakh. The block becomes empty as there are no assets in it. No depreciation will be allowed and the balance of Rs 2 lakh will be treated as terminal depreciation or short term capital loss

e) When the depreciation is allowed on the **actual cost**/ WDV of the assets of the undertakings engaged in generation or destitution of power called power companies, following rules will apply:

- When an asset viz. any building, machinery, plant or furniture in respect of which depreciation is allowed, is sold, discarded, demolished or destroyed in the previous year not being the year in which it is first brought into use, terminal depreciation will be allowed.
- Terminal depreciation is the deficiency or shortfall between the written down value and the sales proceeds / or moneys payable including scrap value, insurance, salvage or compensation moneys payable in respect thereof.
- Terminal depreciation is not allowed in the year in which it was first brought to use.
- Such deficiency must be actually written off in the books of the assessee.
- Any surplus arising therefrom is called the balancing charge and taxed as income u/s 43.
- Any moneys received over and above the depreciation allowed will be treated as capital gains – u/s 50A.
- Under the old laws, actual cost motor cars was restricted to Rs. 25,000, although the actual cost could be higher. In such a case actual cost/deficiency will be taken proportionately in the ratio of actual cost and Rs. 25,000
- Sale includes a transfer by way of exchange or a compulsory acquisition under any law for the time being in force but does not include a transfer, in a scheme of amalgamation.

Illustrations -13

A machine costing Rs 1 lakh is sold for Rs 15,000.
Depreciation of Rs 80,000 was written off on it.

The Written down value of the machine will be Rs.1,00,000-80,000 = Rs 20,000. The deficit of Rs 5,000 or (20,000-15,000) will be the terminal depreciation.

Illustration 14

If the machine is sold for Rs. 90,000, the surplus of Rs 70,000 i.e. (Rs 90,000-20,000) will be the balancing charge-maximum to the extent of depreciation allowed.

Illustration 15:

If the sale price is Rs.1,05,000, then the out of resultant surplus of Rs 85,000 i.e.(1,05,000-20,000), Rs. 80,000 (up to the depreciation allowed) will be the balancing charge and the balance of Rs. 5,000 will be treated as capital gain.

4.3.8 Unabsorbed Depreciation- Section 32(2)

Under section 32 (2), if amount of depreciation cannot be wholly or partly deducted in any previous year because of the lack or inadequacy of profits or gains, the amount of depreciation not deducted is treated as unabsorbed depreciation and allowed to be carried forward to the following previous year and deemed to be part of allowance for that year, and if there is no such allowance for that previous year, be deemed to be the allowance for that previous year, and so on for the succeeding previous years for indefinite period. In other words, the unabsorbed depreciation is treated as part of the current depreciation and can accordingly be set-off against any other head of income even where the business has been discontinued.

Illustration -16

If the depreciation allowable is Rs 80,000 but the profits before depreciation is Rs 50,000, then depreciation of Rs 50,000 will be deducted and the balance of Rs 30,000 will be unabsorbed depreciation.

Illustration-17

Determine taxable income & unabsorbed depreciation :

Particulars	Rs.
Business Income (before depreciation)	10,00,000
Depreciation allowable as per Income Tax Act	16,00,000
Income from other sources	8,00,000

Solution:

Particulars		Rs.
Business Income before depn.	10,00,000	NIL
Less: Depn. to the extent of profits	<u>10,00,000</u>	
Income from other sources	8,00,000	2,00,000
Balance of the current depreciation (16,00,000 - 10,00,000)	<u>6,00,000</u>	
Taxable Income	Rs.	2,00,000

Illustration-18:

Assume depreciation is of Rs. 20,00,000 in above case.

Solution:

Particulars		Rs.
Business Income before Depn.	10,00,000	NIL
Depreciation to the extent of profits	<u>10,00,000</u>	
Income from other sources	8,00,000	NIL
Unabsorbed Depreciation for the current year to the extent of income	<u>8,00,000</u>	
Taxable Income	Rs.	NIL
Unabsorbed Depreciation to be carried forward to next year	Rs.	2,00,000

Illustration-19:

Ascertain value of block on 31-03-2018 from the following:

A. Written down value on April 1, 2017

Particulars & Dep Rate)	Rs.
Plant A,B & C -15%	1,00,000
Plant D & E – 40%	2,60,000
Plant F – 50%	70,000
Building A & B -10%	2,00,000
Building C&D - 5%	7,00,000
Building E -Temporary Sheds E -100%	8,00,000

B. Purchase during the previous year 2017-18

Date	Particulars	Rs.
02/04/2017	Plant G -50%	60,000
01/05/2017	Plant H-15%	18,000
01/06/2017	Furniture-10%	60,000
01/08/2017	Building G- 5%	5,00,000
01/09/2017	Computer-60%	1,00,000
01/10/2017	Franchise Rights -25%	10,00,000

C. Sales during the previous year 2015 -16

DATE	PARTICULARS	(RS.)
31/10/2017	Plant C	25,000
31/01/2017	Plant D	15,000
01/06/2017	Furniture	50,000
06/03/2018	Building E	2,00,000

Temporary sheds were put to use in the previous year.

Solution**Computation of Depreciation / Cost of Block**

Block	Rate	Block 1/04/17	Purchase	Sales	Block	Dep.	Block 31/03/18
Plant A/B/C	15%	1,00,000	18,000	25,000	93,000	13,950	79,050
Plant D/E	40%	2,60,000	-	15,000	2,45,000	98,000	1,47,000
Plant F/ G	50%	70,000	60,000	-	1,30,000	65,000	65,000
Building A& B,	10%	2,00,000	-	-	2,00,000	20,000	1,80,000
Building C/D /G	5%	7,00,000	5,00,000	-	12,00,000	60,000	11,40,000
Building E	100%	8,00,000	-	2,00,000	6,00,000	0	0
Furniture	10%	-	60,000	50,000	10,000	0	0
Computer	60%	-	1,00,000	--	1,00,000	60000	40,000
Franchise rights	25%	-	10,00,000	-	10,00,000	2,50,000	7,50,000

Note: The block of temporary sheds ceases to exist. Hence no depreciation will be allowed and the balance of Rs 6,00,000 will be treated as short term capital loss. Similarly, no depreciation will be allowed on furniture purchased and sold in the same year.

Illustration-20

Opening balance in a certain block of assets consisting of three cars (rate of depreciation @ 20%) is Rs. 18,00,000. During the year 2017-18, new car is purchased for Rs. 6,00,000 and an old vintage car was sold for Rs. 24,00,000. Compute depreciation for A.Y. 2018-19.

Solution**Computation of the value of Net Block**

Particulars	Rs.
Opening WDV of block-3 Cars)	18,00,000
Add: cost of new car purchased	6,00,000
Total-4 cars	24,00,000
Less: sales price -1 car Sold	24,00,000
Closing Balance of block -3 cars	0
Depreciation allowable Because WDV is nil <i>although three cars still exist in the block</i>	0

Illustration-21

What would be the position, if all of the above four cars were sold for Rs. 2,00,000 ?

Solution**Computation of the value of Net Block**

Particulars	Rs.
Opening WDV of block-3 Cars)	18,00,000
Add: cost of new car purchased	6,00,000
Total-4 cars	24,00,000
Less: sales price -4 cars sold	20,00,000
Closing Balance -No Cars	4,00,000
Depreciation allowable (empty block)	0
Short term capital loss on sale of cars	4,00,000

4.4. Expenditure on Scientific Research –(Sec. 35)

As per section 43(4), scientific research” mans “*any activity for the extension of knowledge in the fields of natural or applied sciences including agriculture, animal husbandry or fisheries*”. Following amounts are exempt under section 35.

A. Expenditure on inhouse Research relating to own business -Ss. 35(1)(i) ,(iv) and 35[2]

Expenditure) incurred by the assessee on in-house research relating to his own business. Following point ae important.

1. Expenses include –

- Revenue expense,

- Capital expense such as plant or equipment for research or construction of building (excluding cost of land) for research or other expenses of capital nature connected with the research,
 - Capital and revenue expenses incurred up to three years prior to the commencement of business including salaries of the research staff or research material used in scientific research; and the deduction will be allowed in the previous year in which the business is commenced.
2. Expenses should be incurred in relation to assessee's own business. Expenses *not related to assessee's own business would not be allowed*.
 3. Deduction is available, *even if the relevant asset is not put to use for research and development during the previous year*.
 4. An asset used in scientific research covered u/s 35, is not eligible for depreciation. However, depreciation will be allowable, when the asset is put to use for business after cessation of scientific research.
 5. If a scientific research asset is sold:
 - sales price of the asset or amount allowed as deduction u/s 35, whichever is less, will be treated as business income of the previous year in which the sale took place [section 41(3)], and
 - the excess of sale price over cost (or indexed cost) of acquisition will be treated as "Capital gains".

Illustration -22

AB Ltd incurs expenses on scientific research related to its business during the financial years 2012-13 onwards @ Rs 1 Lakh per year. It commences the business during the financial year 2017-18.

The amount allowable as deduction u/s 35. Will be Rs 4 lakh being the aggregate expenditure incurred in F.Y. 2017-18 (year of commencement of business) and three preceding years viz. 2013-14, to 2016-17 is to be allowed as deduction u/s 35 in A.Y.2018-19. Expenditure incurred in F.Y. 2012-13 & 2013-14 will be ignored.

Illustration -23

If a scientific research asset purchased on 01-01-2015 at a cost of Rs. 5 lakh, on which full deduction was allowed u/s 35 in A.Y. 2015-16 is sold on 31/03/2018 for Rs. 7 lakh, Rs 5 lakh being the amount of original deduction allowed, will) ill be charged as the business income and excess over the cost Rs. 2 lakh will be chargeable as capital gain in A.Y. 2018-19.

B. Sum paid for research to others -Sec -35(1)(ii)

an amount equal to **one and one half** times of any sum paid to a research association which has as its object the undertaking of scientific research or to any university, college or other institution approved to be used for scientific research

C. Sum paid to a R &D company – Sec. 35(1)(iia)

Any sum paid to a scientific R&D company registered in India and approved by the prescribed authority to be used by it for scientific research

D. Sum paid for social sciences etc.- Sec. 35(1)(iii)

Any sum paid to any approved research association which has as its object the undertaking of research in social science or statistical research or to a university, college or other institution to be used for research in social science or statistical research.

E. Sum paid for approved research - Sec. 35(1)(iii)

A sum equal to **One and one-half** times of the sum paid by an assessee to a National Laboratory or a University or an Indian Institute of Technology or a specified person with a specific direction that the said sum shall be used for scientific research undertaken under a programme approved in this behalf by the prescribed authority.

F. Approved inhouse Research in drugs, bio- technology etc. -S 35(2AB)(a)

A sum equal to **one and one-half** times of the capital or revenue expenditure (**except on land & Building**) incurred on scientific research (clinical drug trial, obtaining approval from any regulatory authority under law and filing an application for a patent);

- by a **company** (not allowed to other assessees)
- engaged in the business of
 - **bio-technology or**
 - **manufacture or production of any article or thing**, not being an article or thing specified in the XI Schedule),
 - **in-house research & development facility** approved by the prescribed authority subject to the condition that the company enters into an agreement with it for co-operation in such research and development facility and fulfils such other prescribed conditions with regard to maintenance of accounts and audit thereof and furnishing of reports.

Some other relevant points

1. Goods specified schedule XI include beer, wine & other alcoholic spirits, tobacco products like cigars , cheroots, cigarettes, biris, smoking mixtures for pipes and cigarettes, chewing tobacco, snuff , cosmetics and toilet preparations, tooth paste, dental cream, tooth powder, soap, aerated waters,

confectionery, chocolates, gramophones, record-players, projectors, photographic apparatus and goods, office machines and apparatus such as typewriters, calculating machines, cash registering machines, cheque writing machines, intercom machines and teleprinters but NOT Computers, furniture, made partly or wholly of steel, safes, strong boxes, cash and deed boxes, strong room doors, latex foam sponge, polyurethane foam, crown corks, and other fittings of cork.

2. Cost of building will be eligible for deduction u/s 35(2).
3. The expenditure, on which weighted deduction is allowed under this section, will not be eligible for deduction under any other provisions of the Act.
4. "Expenditure on scientific research", in relation to drugs and pharmaceuticals, shall include expenditure incurred on clinical drug trial, obtaining approval from any regulatory authority under any Central, State or Provincial Act and filing an application for a patent.

G. Other important provisions :

- (a) Scientific research by at the approved institutes *need not be related to the business of the assessee*
- (b) Contribution eligible for weighted deduction under this section will not be eligible for deduction under other provisions of the Act.
- (c) In case of any subsequent cancellation or withdrawal of approval to a notified university, college, research association or other institution or any approved programme is withdrawn, weighted deduction will not be denied to the assessee.
- (d) Any violation of condition for approval will result into withdrawal of the deduction as a mistake apparent from record.
- (e) On amalgamation the provisions will continue to apply to the amalgamated company as if the amalgamating company had not sold or otherwise transferred the asset.

4.5. Amortisation of Spectrum Fee -Section 35ABA

Any capital expenditure incurred for acquisition of any right to use spectrum for telecommunication services will be deducted equally over a period of the expenditure.

4.6. Amortisation of licences Fee -Section 35ABB

Any capital expenditure incurred for obtaining licence by a telecommunication operator will be deducted equally over a period of the expenditure.

Common provisions

- The deduction in respect of licence fees or spectrum fees may be withdrawn as wrongly allowed as a mistake apparent from record in case of non-compliance of provisions like transfer of spectrum or licence.
- On amalgamation, the provisions will continue to apply to the amalgamated company as if the amalgamating company had not sold or otherwise transferred the asset

Illustration

Vodafone pays 4G fees of Rs 50 Cr. with a validity of 10 years. Vodafone will be allowed to amortize the fees $1/10 \times 50$ or Rs 5 Cr every year beginning from the year of actual payment or commencement of business whichever is later. In case of amalgamation with Idea, the deduction will be allowed to Idea as if no transfer has taken place.

4.7. Specified infrastructure projects Sec 35AD. (1)

A deduction will be allowed to an assessee in respect of the **capital expenditure** incurred, wholly and exclusively, for any specified business carried on by him in the year in which such expenditure is incurred or the year of commencement of operations in the case of the expenditure incurred prior to the commencement of its operations if the amount is capitalised in his books of account. The provisions like continuance of application of provisions on new entity in case of amalgamation, transfer of hotels etc. and withdrawal of deduction for non-compliance are applicable *mutatis mutandis*. One additional condition is business must be new and not restructure of old business.

Specified business includes:

- i) setting up and operating a cold chain facility;
- (ii) setting up and operating a warehousing facility for storage of agricultural produce;
- (iii) laying and operating a cross-country natural gas or crude or petroleum oil pipeline network for distribution, including storage facilities being an integral part of such network;

- (iv) building and operating, anywhere in India, a hotel of two-star or above category;
- (v) building and operating, anywhere in India, a hospital with at least one hundred beds for patients;
- (vi) developing and building a notified housing project under a scheme for slum redevelopment or rehabilitation framed by the Government;
- (vii) developing and building a housing project under a notified Government scheme for affordable housing;
- (viii) production of fertilizer in India;
- (ix) setting up and operating notified or approved an inland container depot or a container freight station;
- (x) bee-keeping and production of honey and beeswax;
- (xi) setting up and operating a warehousing facility for storage of sugar;
- (xii) laying and operating a slurry pipeline for the transportation of iron ore;
- (xiii) setting up and operating a notified semi-conductor wafer fabrication manufacturing unit ;
- (xiv) developing or maintaining and operating or developing, maintaining and operating a new infrastructure facility viz :-
 - (i) a road including toll road, a bridge or a rail system;
 - (ii) a highway project including housing or other activities being an integral part of the highway project;
 - (iii) a water supply project, water treatment system, irrigation project, sanitation and sewerage system or solid waste management system;
 - (iv) a port, airport, inland waterway, inland port or navigational channel in the sea.

4.8. Exp. on agricultural extension project.-S. 35CCC

An assessee shall be allowed a deduction of a sum equal to **one and one-half times** of the expenditure incurred on notified agricultural extension project. The amount so deducted be deduction shall not be allowed again under any provisions of the Act for the same or any other assessment year.

4.9. Exp. on skill development project .-S. 35CCD

An company assessee (other assesseees excluded) shall be allowed a deduction of a sum equal to **one and one-half times** of the expenditure, capital or revenue, (not being cost of land & building) incurred on notified skill development project. The amount so deducted be deduction shall not be allowed again under any provisions of the Act for the same or any other assessment year.

4.10. Amortisation of Preliminary Expenses-S 35D

The provisions of section 35 D for Amortisation of Preliminary Expenses are summarised as under:-

A. Eligible assessee :

- a) an Indian company, or
- b) a resident non-corporate assessee.

A foreign company (regardless of its residential status and a non-resident or N.O.R non company entity are not eligible under this section

B. Time and purpose of preliminary expenses –

1. For Setting up an undertaking or business BEFORE commencement of business; or
2. in connection with:
 - a) extension of an industrial undertaking; or
 - b) setting up **a new industrial** unit,

AFTER commencement of business.

Expenses incurred after commencement of business, in connection with extension of or setting up a non-industrial undertaking will not be eligible.

C. Eligible Expenditure:

- (a) Expenditure in connection with:
 - preparation of feasibility report,
 - preparation of project report,
 - conducting a market survey (or any other survey necessary for the business of the assessee) or
 - engineering services related to the business of the assessee, carried out by the assessee himself or by a concern approved by the CBDT.
- (b) Legal charges for drafting any agreement for setting up or conduct of the business.
- (c) Legal charges for drafting the Memorandum and Articles of Association. (M/A)
- (d) Printing expenses of the Memorandum and Articles.
- (e) Registration fees of a company under the Companies Act.
- (f) Expenses in connection with the public issue of shares or debentures of a company, underwriting commission, brokerage and charges for drafting, typing, printing and advertisement of the prospectus.
- (g) Any other prescribed expenditure.

D. Qualifying Expenditure:

The aggregate expenditure exceeding the following limits will not be eligible for deduction under this section :-

- a) corporate assessee - Higher of the following :
 - 5% of cost of project; or
 - capital employed, whichever is more
- b) non-corporate assessee: 5 per cent of cost of project

E. Definitions of the terms**(i) Cost of project:**

Cost of project means the aggregate of actual cost of fixed assets appearing in the books of the assessee as on the last day of the previous year in which the business of the assessee commences.

Fixed assets include land, buildings, leaseholds, plant, machinery, furniture, fittings and railway sidings (including expenditure on development of land and buildings), or additional cost incurred after commencement of business in connection with extension or setting up an industrial undertaking) of fixed assets,

(ii) Capital employed –

Capital employed means the aggregate of the -

- issued share capital,
- debentures, and
- long-term borrowings,

as on the last day of the previous year in which-

- the business of the company commences, or
- additional capital borrowings etc. brought after commencement of business in connection with extension or setting up an industrial undertaking,

Long term borrowings for this purpose means moneys borrowed in India by any company from the Government or Financial institutions like ICICI, IFCI etc. or banks or foreign borrowings in connection with acquisition of plant and machinery repayable after a term of seven years or more.

F. Amount of deduction:

One-fifth of the qualifying expenditure is allowable as deduction in each of the five successive years beginning from the year of -

- commencement of the business, or
- completion of extension of industrial undertaking , or
- commencement of production or operations by the new industrial unit.

G. Other Points:

1. Non- corporate assesseees are required to get their account audited for claiming deduction under this section.
2. On amalgamation/ demerger of the assessee company with other company, deductions can be claimed by the amalgamating or demerged company.
3. Amount deducted under this section will not be eligible for deduction under any other provision of the Act.

Illustration -24

ABC Ltd is an existing Indian company engaged in developing and providing computer software services. It incurs the following expenditure in connection with the setting up of a new unit. The project is complete in March 2018. Determine the amount deduction admissible u/s 35D.

Particulars	Rs
Preparation of project report	2,00,000
Market Survey	6,00,000
Legal charges for additional capital for new unit	3,00,000
Engineering services not approved by CBDT	5,00,000
Cost of the Project as on 31/03/2018*	60,00,000
Capital employed as on 31 -03-2018	50,00,000

Solution:**Eligible Expenditure:**

Particulars	Rs
Preparation of project report	2,00,000
Market Survey	6,00,000
Legal issue of additional capital for new unit	3,00,000
Engineering services not approved- ineligible	0
Total	11,00,000

Gross Qualifying Amount:

5% of cost of the project- (5% X 60,00,000)	3,00,000
5% of the capital employed (5% X 50,00,000)	2,50,000
Gross Qualifying Amount (higher of the two)	3,00,000

Qualifying Amount:

Net qualifying amount Rs 3,00,000 being the lower of the following:

- I. Gross qualifying amount :Rs 3,00,000 or
- II. Actual amount of preliminary expenses: Rs 11,00,000

Amount of Deduction:

$\frac{1}{5}^{\text{th}}$ of the net qualifying amount ($\frac{1}{5} \times 3,00,000$) Rs. 60,000 each for 5 assessment from A.Y. 2018-19 onwards.

4.11. Exp. on amalgamation/ demerger - S. 35DD.

U/s 35DD, any expenditure incurred wholly and exclusively for the purposes of amalgamation or demerger of an undertaking, the assessee, being an Indian company shall be allowed a deduction of an amount equal to one-fifth of such expenditure for each of the five successive previous years beginning with the year of the amalgamation or demerger. No deduction shall be allowed in respect of such expenditure under any other provision of this Act.

4.12. Exp. Under VRS - S. 35DDA

U/s 35DDA **one fifth** of the payment made to an employee in connection with his voluntary retirement under any VR Scheme by an assessee is deducted in the year and four consecutive years each thereafter. In case of amalgamation/ demerger/ reorganisation (from one entry to another) of a company assessee, the deduction will be available to the amalgamated / resultant company or the successor entity . No deduction shall be allowed in respect of such payment under any other provision of this Act

4.13. Exp. on prospecting, etc., for minerals – S. 35E

U/s 35E one $\frac{1}{10}$ of expense incurred on prospecting of specified minerals or any deposits thereof incurred by an Indian company or a resident non-company assessee engaged in mining operations are debited equally in 10 instalment beginning from the year of commencement of the commercial production .

Other relevant points:

- (i) Such expenses should be incurred in the year of commercial production or immediately preceding four years.
- (ii) Expense will not include the following;
 - a. Any part of expenses met directly or indirectly by any other person or authority;
 - b. any sale, salvage, compensation or insurance moneys realised by the assessee in respect of any property or rights brought into existence as a result of the expenditure;

- c. any capital expenditure for acquisition of the mines or deposits of such mineral or any rights therein
- (iii) operation include exploring, locating or proving deposits of any mineral, and includes any such operation which proves to be infructuous or abortive.
- (iv) Non- company assesseees are required to get their account audited and furnish the report thereof along with the return of income
- (v) Provision for continuance in case of amalgamation, merger, demerger, restructure of business or conversion of one entity to another are also applicable as per the section mutatis mutandis
- (vi) In case of inadequacy of profits , the unabsorbed amount will be added in next year's claim and so on up to the tenth previous year from the year of commercial production.

4.14. Specific deductions: - Section. 36

Section 36(1) expressly allows the following specific deductions in computing taxable income under the head profits and gains of business or profession:

4.14.1. Insurance premium –Sec. 36(1)(i)/(ia)/(ib)

Any amount of any insurance premium paid

- To cover risk of damage or destruction of *business stocks used in business or profession*; - S. 36(1)(i)
- on the *life of the cattle* owned by the milkmen being member of a primary co-operative society, by a federal milk co-operative society- S. 36(1)(ia)
- on the *health of his employees* by an employer , paid by any mode of payment other than cash (e. g. cheque) an approved scheme framed by the GIC or other insurer approved by the IRDA)- S. 36(1)(ib)

4.14.2. Bonus or commission- S. 36(1)(ii):

Any sum paid to an employee as *bonus or commission* for services rendered, where such sum would not have been payable to him as profits or dividend if it had not been paid as bonus or commission. U/s 43B, bonus or commission will be deducted only on payment thereof on or before the due date of furnishing return u/s139.

4.14.3. Interest on capital borrowed - S. 36(1)(iii):

Interest paid or payable on borrowed funds used for the purpose of business or profession.

Borrowed funds include recurring subscriptions paid periodically by shareholders / subscribers in Mutual Benefit Societies, which fulfill the prescribed conditions is deemed to be capital borrowed .

Interest (paid/payable in respect of capital borrowed for acquisition of an asset for extension of existing business or profession whether capitalized in the books of account or not) will be allowed only when an asset is put to use.

Interest for the period from the date of borrowing till the date when the asset is put to use will not be allowed but be added to the cost of the asset. This is in harmony with ICDS- IX, which mandates commencement of capitalization of interest from the date of borrowing of funds till the asset is first put to use, irrespective of whether acquisition of the asset is for extension of existing business or not.

4.14.4. Zero Coupon Bonds- S. 36(1)(iiia):

Discount on notified (by Central Government) Zero Coupon Bonds issued by an infrastructure capital company or infrastructure capital fund or a public sector company is allowable on *pro rata* basis provided no other benefit or payment is received in respect of such bonds before their maturity.

Zero Coupon Bonds are the bonds, which do not carry coupon rate of interest. Instead, the bonds are issued at a price lower than their redemption value. The difference between issue price and redemption value or the discount is allowed as deduction on *pro rata* basis having regard to the period of life i.e. date of issue to the date of maturity or redemption of such bonds. Briefly, discount on Zero Coupon is amortised over the life time of the Bonds.

Illustration-25:

Infrastructure Capital Company issues 1 Crore duly notified Zero Coupon Bonds of Rs. 1000 each at a price of Rs. 640 on 01/01/2016. The bonds are redeemable at par on 31/12/2018. Show how the discount would be deducted from the total income of the company.

Solution:

Face value of Bond- Rs 1,000

Issue price - Rs 640

Discount offered Rs 1000-640 = Rs 360

Total discount offered on 1 Crore bonds- Rs. 360 Crore

The tenure of the coupon is three years or 36 months.

Pro rata deduction to be allowed

A.Y. 2016-17- 3 months (01/Jan-2 016 31March 2016)	3/36X360Cr	Rs.30Cr.
A.Y. 2017-18 -12 Months	12/36X360Cr	Rs120Cr.
A.Y. 2018-19 -12 Months	12/36X360Cr	Rs120Cr.
A.Y.2019-20 -9 months April 31--Dec.31,2018 =9 Mon	9/36X360Cr	Rs 90Cr.

4.14.5. Contribution towards RPF / approved superannuation fund -S. 36(1)(iv):

Any contribution paid by the assessee as an employer towards a recognised provident fund/ approved superannuation fund, subject prescribed limits and conditions and also subject to the provisions of S 43B.

4.14.6. New Pension Scheme- (Sec- 36(1)(iva) :

Any contributions by employer to a pension scheme referred to in Section 80CCD(2) on account of employee to the extent of 10% of his salary plus dearness allowance but excluding all other all other allowances and perquisites.

4.14.7. Approved gratuity fund- Sec. 36(1)(v):

Any sum paid by the assessee as an employer by way of contribution towards an approved gratuity fund created by him for the exclusive benefit of his employees under an irrevocable trust;

4.14.8. PF/ESIC -Sec. 36(1)(va)

Contribution received by an employer from his employees for crediting in any fund e.g. P.F. or ESIC and credited by the assessee to the employees' account in the relevant fund or funds on or before the due date prescribed under the relevant law.

Such contributions from employees are treated as income of the employer u/s 2(24)(X) when received and allowed as deduction when paid by the due date in terms of Sec 43B.

4.14.9. Death of animals-- S. 36(1)(vi)

The difference between the actual cost to the assessee of the animals and the amount, if any, realised in respect of the carcasses or animals used for the purposes of the business/ profession otherwise than as stock-in-trade but died or become permanently useless for such purposes,

Where the animals are treated as stock in trade, the loss or profit is the part of normal sales and purchase, therefore this provision is not applicable.

4.14.10. Bad debts- S. 36(1)(vii)

Under Sec S. 36(1)(vii) and Sec 36(2) , any amount of bad debt or part thereof, which is written off as irrecoverable in the accounts

of the assessee for the previous year is allowable subject to following conditions -

- (a) There is relationship of debtor and creditor.
- (b) The debt is incidental to the business or profession.
- (c) The debt has been considered in the computation of income, or it represents money lent in ordinary course of the business of banking or money-lending.
- (d) Bad debt is written off as irrecoverable in assessee's accounts in the previous year
- (e) Any debt written off but not allowed earlier may be deducted as bad debts
- (f) Bad debts will not include any provision for bad and doubtful debts made in the accounts of the assessee;
- (g) Any deficiency will be deductible in the previous year in which the ultimate recovery is made;
- (h) any such debt or part of debt written off as irrecoverable in an earlier previous year may be deducted if the deduction was not allowed on the ground that it had not been established to have become a bad debt in that year;
- (i) The assessing officer may deduct bad debts written off in the current year ; in an earlier previous year u/s 155(6) within a period of 4 years if he is satisfied that the debt became irrecoverable in earlier years .
- (j) A bad debts can be claimed without recording in books of account as irrecoverable or bad as per second proviso to section 36(1)(vii) if the debt was considered in the computation of income as per the notified ICDSs.

4.14.11. Provision by banks-Sec. 36(1)(vii):

U/s 36(1)(vii) deduction is allowed to Indian scheduled & non-scheduled banks, financial institutions and non-banking financial companies in respect of provision for bad and doubtful debts upto the following limits namely :-

- 8.5% of total income by a scheduled Indian bank other non-scheduled bank,
- 5% of total income a public financial institution or a State financial corporation or a State industrial investment corporation and a foreign bank of the total income (computed before making any deduction under this clause and Chapter VI-A), and
- 10% of the aggregate average advances made by the rural branches of such bank computed in the prescribed manner, and subject to certain conditions, or

- 5% of total income of a non- banking financial company;
- 5% of Non-Performing Assets or NPAS in accordance with the RBI guidelines shown in the books of account of the bank on the last day of the previous year a bank at the option of the bank.

The deduction is subject to two conditions :

- (a) Assessee has debited the amount of such debt or part of debt in that previous year to the provision for bad and doubtful debts account .
- (b) Deduction relating to any such debt or part thereof shall be limited to the amount by which such debt or part thereof exceeds the credit balance in the provision for bad and doubtful debts account .

4.14.12. Special reserve-- S. 36(1)(viii)

Under Sec 36(1)(viii) financial institutions are entitled to a deduction upto 40% of their profits in respect of amounts transferred to a special reserve created and maintained by them subject to a ceiling of twice the amount of the paid-up share capital and of the general reserves.

Financial corporation mean

- a corporation which is engaged in providing long-term finance for industrial, agricultural development or development of infrastructure facility in India ,or
- a 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,

Profit means profits derived from such business of providing long-term finance computed under the head Profits and gains of business or profession before making any deduction under this clause

4.14.13. Promotion of family planning - S. 36(1) (ix)

Vide Sec 36(1)(ix)- expenditure incurred *bona fide* by a company for promotion of family planning amongst employees -

- in full, if the expenditure is of revenue nature; and
- One fifth of capital expenditure for each of the five years beginning from the year in which it was incurred.

Unabsorbed family planning expenditure will be allowed to be carried forward and set off in the same manner as depreciation.

4.14.14. Exp . by Statutory bodies - S. 36(1)(xii):

Under Section 36(1)(x), revenue expenditure incurred, by any statutory corporation or a body corporate for the objects and

purposes authorised by the Act under which it is constituted or established will be deductible.

4.14.15. Cash Transaction Tax- S. 36(1)(xiii):

Any amount of banking cash transaction tax paid by the assessee is deductible u/s 36(1)(xii):

4.14.16. Credit Guarantee Fund -Sec. 36(1)(xiv)

Any sum paid by a public financial institution by way of contribution to a specified credit guarantee fund trust for specified small industries will be deductible u/s 36(1)(xiv).

4.14.17. Security Transaction Tax -S. 36(1)(xv):

The security transaction tax (STT) paid by the assessee will be deducted u/s 36(1)(xv), if the income arising from taxable securities transactions is included in the income computed under the head "Profits and gains of business or profession.

4.14.18. Commodity Transaction Tax S. 36(1)(xvi):

The commodity transaction tax paid by the assessee will be deducted u/s 36(1)(xvi), if the income arising from such taxable commodity transactions is included in the income computed under the head "Profits and gains of business or profession.

4.14.19. Expenditure by Co-operative Society for purchase of Sugarcane [Sec 36(1)(xvii)]

The expenditure incurred by a co-operative society engaged in the business of manufacture of sugar for purchase of sugarcane at a price, which is equal to, or less than the price fixed or approved by the Government, will be allowed as a deduction under Sec 36(1)(xvii).

4.14.20. Losses as per IDCDS-[Sec 36(1)(xviii)]

Marked to market loss or other expected loss as computed in accordance with the notified income computation and disclosure standards

5. GENERAL DEDUCTIONS– S. 37:

Section 37 is the residual section, which provides for deduction of all the expenditure as under :-

- (a) The expenditure should be incurred *wholly and exclusively for the purposes of the business/ profession* carried on by the assessee, in respect of which income is computed under this head.
- (b) The expenditure, subject to the provisions of Section 43B, should be incurred during the previous year;

- (c) *expenses should be incurred after the business or profession is set up*
- (d) *Expenses must be revenue expenses in nature e.g. expenses by way of cost of raw materials, tools, spares , cost of labour, salary , brokerage, commission, legal fees, litigation expenses, professional tax, trade mark registration, lease rent or other business expenses incurred by the assessee.*
- (e) The section excludes some expenses. Such expenses will not be allowed under this section. A list of such expenses is as under :-
 - i. Capital expenditure e.g. expenditure on acquisition or renovation of assets , conveyance or registration of land, eviction of a tenant etc. ;
 - ii. Personal expenses e.g. income tax or wealth tax, drawings or household expenses of the assessee;
 - iii. Expenses expressly allowed in Ss. 30 to 36;
 - iv. Expenses incurred for any purpose which is an offence, or which is prohibited by law, e.g. penalty, bribery, composition money paid in respect of any offences or breach of law or penal interest under any law etc.
 - v. Expenses on advertisement in any souvenir, brochure, tract, pamphlet or the like published by a political party specifically excluded from the purview of the section - S. 37(2B)
 - vi. any expenditure incurred by an assessee on the activities relating to corporate social responsibility referred to in section 135 of the Companies Act, 2013

6. SPECIFIC DISALLOWANCES– S.40-40A-43B

6.1. Some expenses are not allowed be deducted while computing the business income for a number of reasons such as :-

- Not satisfying the inherent conditions attached with the allowance. E.g. Personal and capital expenses will be disallowed u/s 37, which allows only revenue expenses incurred wholly and exclusively in the course of business or profession.
- Absolute disallowances for policy reasons such as political advertisement and CSR expense, which are expressly disallowed u/s 37.
- Defaults such as non-deduction of tax at source.
- Deferment or time factor. E.g., Unpaid taxes, bonus etc. covered u/s 43B are disallowed in the year of accrual.

- Personal element, e.g., drawings by an individual, interest and remuneration in case of a firm.
- Reasonableness e.g. unreasonable payments to relative u/s 40A(2),
- Mode for payment e.g. Cash payments u/s 40A (3)
- Partial disallowance due to ceilings, e.g. interest and remuneration payable to partners.
- Express disallowance , e.g. CST expenses
These disallowances are discussed below

6.2. Disallowance in case of any assessee – S. 40(a)

1. *Payments to Non-Residents without TDS* [S. 40(a)(i)]

Any interest, royalty, fees for technical services or other sum chargeable under this Act, which is payable —

(A) outside India; or

(B) in India to a non-resident, not being a company or to a foreign company, on which tax is deductible at source and such tax has not been deducted or, after deduction, has not been paid on or before the due date for filing return of income u/s 139 (1).

The amount so disallowed will be allowed as a deduction in computing the income of a subsequent previous year in which such tax has been paid.

Illustration-26.

A pays commission of Rs. 1,50,000 to a Non-Resident for the previous year 2017-18, on which tax of Rs 30,000 is required to be deducted. Show whether the commission will be allowable in the following situations.-

- a) A does not deduct tax at source at all.
- b) A deducts tax at source but does not pay the tax to the Government in time.
- c) A deducts tax at source but not and pays it to the Government in time.
- d) A pays the tax to Government after deducting the same in December 2018

Solution:

In cases (a) and (b) commission will be disallowed u/s 40(a)(i) because the assessee fails to deduct the TDS or pay the amount of TDS to the Government.

In case(c) deduction will be available in A.Y. 2018-19.

In case (d), deduction will be allowed in A.Y. 2019-20.

2. Payments made to residents without TDS [S.40(a)(ia)]

30% of any sum paid or payable to a resident, on which tax is deductible at source and such tax has not been deducted or, after deduction, has not been paid on or before the due date for filing return of income u/s 139 (1) shall be disallowed u/s 40(a)(ia)

Such disallowance will not be made if the recipient of the income has paid the due tax thereon and as a result thereof the assessee is not deemed to be an assessee in default U/s 201(1).

However, the sum so disallowed (30%) will be allowed as a deduction in computing the income of a later previous year in which such tax has been paid:

3. Payment on account of fringe benefit tax, [S. 40(a)(ib)]:

4. Any sum paid on account of any rate or tax levied on the profits or gains of any business/ profession or assessed at a proportion of, or otherwise on the basis of, any such profits or gains.-[S. 40(a) (ii)];

5. Payment on account of *wealth-tax*, [S. 40(a) (ia)]

6. Any amount paid by way of royalty, licence fee, service fee, privilege fee, service charge or any other fee or charge, by whatever name called, which is levied exclusively on; or which is appropriated, directly or indirectly, from, a State Government undertaking by the State Government, [S. 40(a) (iib)]

7. *Salary payable outside India* or to a non-resident, and if the tax has not been deducted or deducted and has not been paid therefrom under Chapter XVII-B.

However, such salaries will be allowed as a deduction in the year in which the tax has been paid in respect of the salary, [S. 40(a) (iii)]

8. Any payment to a provident or other fund established for the benefit of employees of the assessee, unless the assessee has made effective arrangements to secure that tax shall be deducted at source from any payments made from the fund, which are chargeable to tax under the head Salaries. Such payment will not be allowed as a deduction if tax has not been deducted in the year in which such payments have been made. However, these payments will be allowed as a deduction in the year in which tax has been paid.[S.40(a) (iv)]

8 Any tax actually paid by an employer on perquisites u/s10, (10CC)-[S. 40(a) (v)]

6.3. Disallowances in the case of any firms- S.40(b)

a. *Remuneration to partners*– S. 40(b)

Following are the provision about remuneration payable to partners of a firm assessable as such namely.-

- (i) Any payment of remuneration to any partner ,
 - a. who is **not a working partner**; or
 - b. who is a **working partner**, but such payment of remuneration is **not authorised** by, or is not in accordance with, the terms of the partnership deed;
 - c. a working partner but payment of remuneration though authorised, relates to any period falling **prior to the date of such partnership deed** or

For this purpose, “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;

- (ii) any payment of remuneration, to a working partner though authorised and otherwise allowable, if the remuneration to all partners in aggregate exceeds the following limits:

Book Profits	Remuneration allowable
on the first Rs. 3,00,000 of the book profit or in case of a loss	Rs.1,50,000 or 90 % of the book-profit, whichever is more;
on the balance of the book-profit	60 % of the book profits

“*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 deducted while computing the net profit. In other words, Book Profit means net profit before providing for remuneration to partners.

“*Remuneration* means “any payment of salary, bonus, commission or remuneration by whatever name called.

b. *Interest to Partners*-S. 40(b)

- (i) Any payment of *interest* to any partner which is *not authorised by* or is not in accordance with, the terms of the partnership deed; or
- (ii) *Interest*, to partner though authorised, relating to any *period falling prior to the date* of such partnership deed, or

(iii) Interest in accordance with the deed of partnership but in excess of the amount calculated at the rate of twelve per cent simple interest per annum;

Following points are also relevant in this regard:-

(i) A partnership deed may, at any time during the said previous year be amended to provide for payment of interest but such amendment will be applicable only prospectively. Retrospective effect cannot be given to such terms.

(ii) The interest will be considered in the same capacity in which it is paid.

Illustration – 27 :

A is a partner in a firm as a trustee of B. A advances his personal money as well as B's money to the firm. The firm pays interest to A in his personal capacity and as the representative or trustee of B.

Interest payable to A in his capacity of trustee will be considered u/s 40(b). Interest paid in his individual capacity will be ignored. On the other hand, if A is a partner in his individual capacity, then interest paid to him in his representative capacity shall be ignored.

Illustration-28:

For the financial year 2017-18, a firm shows net profit of Rs 50,000 after debiting the following amounts:

- Remuneration to A (not a working partner) Rs 50,000.
- b) Remuneration to B- Rs 5,00,000 for the full year. The firm has made provision for his remuneration by a partnership deed dated 01/7/2017
- c) Interest to partners @ 18% p.a. Rs. 90,000.

Compute the business profits for A.Y. 2018-19

Solution:

Computation of Profits from Business -A.Y. 2018-19	
Particulars	Rupees
<i>Business Profits as per P/L A/c</i>	<i>50,000</i>
<i>Add back- Salaries & Interest paid to partners (50,000+5,00,000+90000)</i>	<i>6,40,000</i>
<i>Book Profits before interest & remuneration</i>	<i>6,90,000</i>

<i>Less: Interest authorised by partnership deed restricted to 12% i.e. 90,000 X 12/18</i>		60,000
<i>Book Profit Before Remuneration</i>		6,30,000
<i>Remuneration to Partners (Lowest of the following)</i>		3,75,000
<i>A –(Nor working partner</i>	<i>NIL</i>	
<i>B- Actual Remuneration</i>	<i>5,00,000</i>	
<i>Remuneration allowed from the date of deed - 9 months from 01/07/2017 to 31/03/2018 5,00,000 X 9/12</i>	<i>3,75,000</i>	
<i>Maximum allowable</i>	<i>4,75,200</i>	
<i>90% of Rs 300000 of book profit Rs 2,70,000</i>		
<i>60% of the balance book profit of Rs (6,42,000-3,00,000)- 2,05,200</i>		
<i>Profits from Business</i>		<i>2.55,000</i>

c. Remuneration/Interest by an association of persons(AOP) /body of individuals (BOI)-S. 40(ba):

Any payment of interest, salary, bonus, commission or remuneration, by whatever name called, made by an association of persons (AOP) /body of individuals (BOI) to a member of such association or body.

“Association or “body” does not include a company or a co-operative society or a society registered under the Societies Registration Act, 1860, or other registered charitable trusts).

Following points are also relevant:-

a. Unlike a firm, no part of interest paid to a member is allowable in case of an association or a body. Hence, capacity or status of the member in such AOP or BOI is relevant. Accordingly -

- i. Interest paid by a member in his representative capacity to the association or body or *vice versa* shall be ignored if he is a member in his individual capacity.
- ii. Conversely , Interest paid by a member in his individual capacity to the association or body or *vice versa* shall also be ignored if he is a member in his representative capacity.

- iii. Interest paid by a member in his representative capacity to the association or body or *vice versa* shall be considered if he is a member in his representative capacity.
 - iv. Interest paid by a member in his individual capacity to the association or body or *vice versa* shall be considered if he is a member in his individual capacity
- b.** Where, interest is paid to a member on funds borrowed by him, the disallowances will be only on the net amount receivable by such members.
- c.** Remuneration or interest to members of AOP/BOI are not allowed to be deducted for computing income from business and profession

Illustration-28

X is a member of BOI. X borrows a sum of Rs. 1,00,000 from market with interest rate of 12% and advances it to the BOI. A BOI pays Interest @ 15% p. a. to X. Determine the amount to be disallowed.

Solution:

Particular	Rs
Interest payable by BOI to X 15% on Rs 1,00,000	15,000
Interest payable by X on his borrowing 12% on Rs 1,00,000	12,000
Disallowable u/s 40(b) (Net)	3,000

6.4. Disallowances In the case of all assesses –S.40A

S. 40A provides for disallowance of certain expenses in certain circumstances. Most of these disallowances are anti-avoidance measures in nature and as such are overriding and prevailing. Sec 40A (1) expressly states that:-

“ The provisions of this section shall have effect notwithstanding anything to the contrary contained in any other provision of this Act relating to the computation of income under the head "Profits and gains of business or profession".

The disallowances are discussed as under:-

1. Excessive payment to relatives -S. 40A (2)

U/s 40A(2)(a) Any expenditure resulting in any payment to any specified person may be disallowed to the extent it is excessive or unreasonable in the opinion of the assessing officer having regard to the market value of the goods or services and the benefit to the business or profession.

The section specifically excludes domestic transaction referred to in section 92BA, if such transaction is at arm's length price as defined in 92F(ii).

Sec 40A(2) (b) gives a long list of specified persons , which is summarised as under :-

A. Persons connected with the assessee	
Status of assessee	Specified person
Individual	any relative of the assessee;
Company	any director or his relative
Firm	any partner or his relative
Association of Persons	any member or his relative
Hindu Undivided Family	any member or his relative
B. Sister concerns	
Entity holding substantial interest of the assessee	
<i>Person holding a substantial interest in the business or profession of the assessee</i>	<i>Specified person</i>
Individual	Individual or his relative
Company	any director or his relative
Firm	any partner or his relative
Association of Persons	any member or his relative
Hindu Undivided Family	any member or his relative
C. Persons connected with the sister concerns	
If partner of a firm, or director of company or member of a HUF , AOP hold substantial interest , then such company , firm, AOP or HUF will be the specified person also other directors, partners , members and their relatives will be the specified persons (The above table will be applicable to the concerns of where such persons are partners directors or members)	
D : Reverse connection :	
Where assessee or his relatives, or if the assessee is a company, firm , HUF ,AOP & its directors , members or partners etc. or their relatives), hold substantial interest in the business of other individual, company, firm, AOP or HUF, the latter will be treated as the specified persons .	

“Relative” in this context means husband, wife, and brother, sister or any lineal ascendant or descendent of the individual.

A person holding **“Substantial interest”** means a person holding 20% voting power in a company at any time during the previous year or twenty per cent of the profits of other concern viz proprietary concern, HUF, AOP, BOI etc.

Illustrations -29:

Determine the specified persons u/s 40A (2)

- a. A is an individual. His wife is a specified person
- b. A is a firm having B,C & D as partners, B ,C & D and their relatives will be the specified persons
- c. If A is a HUF with B, C & D as members, B ,C & D and their relatives will be the specified persons
- d. If A is a AOP with B, C & D as members, B, C & D and their relatives will be the specified persons
- e. If A is a Company with B, C & D as directors B, C & D and their relatives will be the specified persons.
- f. In the above cases B is a company, then B and all directors of B will be the specified persons.
- g. If C is a firm, then C and all partners of C will be the specified persons
- h. If D is A HUF or AOP, all the members as well as D will be the specified persons.

2. Payments exceeding Rs 10,000 /35,000 other than by way of crossed cheque or demand draft – S. 40A(3) /(3A)

As per the sections , where in respect of any expenditure, payment exceeding Rs. 10,000 (Rs. 35,000 in cases of payments made for plying, hiring or leasing goods carriages) during a single day is made otherwise than by an account payee cheque drawn on a bank or account payee bank draft, or use of electronic clearing system(ECS) through a bank account, exceeds ten thousand rupees, no deduction shall be allowed in respect of such expenditure.

Following points require attention:

1. The disallowance is on total payment, if it crosses the limit of Rs. 10,000/ 35,000 i.e. on payments of Rs 10,001/ 35,001, or more.
2. Limit of Rs. 10,000/ 35,000 will be considered with reference to the aggregate of all payments made in a single day.
3. If expenditure is allowed in past on the basis of its accrual and subsequently cash payment is made in respect of such liability, in excess of Rs. 10,000/ 35,000, such excess payment will be deemed to be the business profit in the year of payment.
4. Rule 6D gives some exceptions, when disallowance will not be made if the payment exceeding Rs 10,000 /35000 and is made otherwise than by way of crossed cheque / bank draft etc. some of these circumstances are: new buyer, bank holiday, lack of banking facility, etc.

5. S 40A (4) forbids a person to raise an issue in a suit for being offered payment by account payee cheque or draft and not in cash.

Illustration-30:

Audit fee provided during the financial year 2015-16 for Rs. 50,000 is paid by cash on 31.03.2018.

Solution

Audit fee of Rs 50,000 allowed as deduction in A.Y. 2015 -16 will be deemed be the profit of the A.Y. 2018-18, when it was paid cash.

Illustration-31

A makes a payment of Rs. 15,000 by a bearer cheque for purchase of goods and claims that disallowance u/s 40A(3) is not applicable and even if it is applicable, it will be restricted only on Rs. 5,000 being, the amount exceeding Rs. 20,000. Examine his claim.

Solution

If payment in excess of Rs 15,000 is made otherwise than by an account payee cheque or draft etc., entire payment of Rs 15,000 will be disallowed without any basic limit. Bearer cheque and cash are not acceptable modes of payment.

3. Provision for Gratuity-S. 40A (7)

Any provision for payment of gratuity to employee on their retirement or termination of their services for any reason will not be allowed u/s 40A (7). But if such provision is made by contributing to an approved gratuity fund or for payment of gratuity that has become payable during the previous year, will be allowed as deduction.

Hence, gratuity is allowed as a deduction only when it has become due and payable. However, once the provision for gratuity has been allowed as deduction in any year, then any subsequent payment thereof will not be deductible again.

4. Provision for non- statutory funds -S.40A (9)

U/s 40A (9), deduction will not be allowed in respect of any sum paid by the assessee as an employer towards the setting up or formation of, or as contribution to, any fund, trust, company, association of persons, body of individuals, society or other institution for any purpose, except where such sum is paid for the purposes and to the extent provided by or under S. 36(1)(iv)/ (v) or as required by or under any other law for the time being in force like approved provident/gratuity funds etc. However, any *bona fide* sum actually spent out of such fund will be allowed as deduction u/s.40 (10). Further, u/s S.40 (11) assessee will be entitled to receive back the unutilised part of any such fund/assets.

5. Unpaid Liabilities-Sec. 43B

Section 43B provides an exception to the mercantile system of accounting in respect of taxes and other specified expenses, which will be allowed in the previous year, in which they are actually paid irrespective of the previous year in which the liability to pay such sum was incurred by the assessee according to the method of accounting regularly employed by him. The section covers any sums payable by the assessee:-

- (a) by way of tax duty, cess or fee, by whatever name called, under any law for the time being in force, or
- (b) as an employer by way of contribution to any provident fund or superannuation fund or gratuity fund or any other fund for the welfare of employees, or
- (c) as bonus or commission to employees- u/s 36(1)(ii) ; or
- (d) as interest on any loan or borrowing from any public financial institutions i.e. ICICI, IFCI, UTI, IDBI LIC or a State financial corporation or a State industrial investment corporation, in accordance with the terms and conditions of the agreement governing such loan or borrowing , or financial arrangement or
- (e) as interest on any loan or advances from a scheduled bank, a co-operative bank other than a primary agricultural credit society, a primary co-operative agricultural or rural development bank accordance with the terms and conditions of the agreement governing such loan or advances, or
- (f) as an employer in lieu of, any leave at the credit of his employee, or
- (g) as user , to Indian Railways for use of railway assets.

Sec 43B provides will not be applicable if :—

1. The payment is actually made on or before the due date of submission of return of income; and
2. the evidence of such payment is submitted along with the return of income.

In brief Sec .43B provides that

1. Sums accrued and paid within the same previous year would be allowed in that year ;
2. Sums accrued in one year and paid in the following year but before the due date of filing will also be allowed on accrual basis on submission of proof of payment .
3. Other sums will be allowed only on cash basis and not on mercantile basis.

Following table summarises the position:

Application of Section 43B	
Case	Year of Deduction
Accrued and paid in same year	Year of payment/accrual ; as both are same
Paid after the end of the year in which it is accrued but on or before the due date of submission of return of income for that year and the proof of deposit is submitted along with the return of income	year of accrual
Any other time not covered above, or proof not attached with return	Year of payment

Illustration-32

ABC Limited pays Sales Tax for the financial year 2018-19 before 30/09/2018. Determine the assessment year in which the sales tax may be claimed as deduction.

Solution

Tax is paid before due date for filling return of income viz. 30/09/2018. Hence, it will be allowed on accrual basis in A.Y.2018-19.

Illustration-33:

ABC Ltd pays excise duty for the previous year 2017-18 on 01/10/2018. In which assessment year will it be allowed?

Solution

ABC Ltd. pays tax after the due date for filling return of income. Deduction will be allowed only in the year of actual payment year 2018-19 relevant to A.Y. 2019-20.

Illustration -34

Determine the year in which the excise duty will be deducted from the business profits of X Ltd., who made following payment of excise duty in the year 2015-16.

S. No.	Date of payment	Rupees
1	02/05/2017	25,000
2	20/07/2017	65,000
3	16/08/2017	80,000
4	05/12/2017	20,000
5	12/06/2018	40,000
6	02/12/2018	10,000
7	Unpaid	10,000
	Total	2,50,000

Solution

- First four payments due and paid in the same year 2017-18 will be allowed as deduction in A.Y. 2018-19.
- Rs. 40,000 paid on 12/06/2018 paid before the due date of filing return will be allowed as deduction in A.Y. 2018-19 if proof of payment is furnished along with return of income.
- Rs. 10,000 paid on 02/12/2018 is paid after the due date for filing of return for A.Y 2018-19, will be allowed in the year of payment i.e. A.Y.2019-20.
- Unpaid amount of Rs. 10,000 will not be allowed as deduction until it is actually paid.

7. CHARGEABILITY OF PROFITS – SEC. 41

Section 41 provides for taxation of the following : -

a. Cessation of liability- Sec 41(1)

Any amount received or the value of any benefit accruing to the assessee or his successor in business, whether in cash or in any other manner or by way of remission or cessation such liability whether by a unilateral act or otherwise, in respect of any loss, expenditure or trading liability incurred by the assessee and allowed as a deduction in any year will be chargeable as the income of the assessee or the successor in business in the year of receipt of accrual of benefit.

"**successor in business**" means amalgamated company in case of amalgamation with another company , the resulting company in case of demerger , the other firm in case of a firm carrying on a business or profession is succeeded by another firm,

Illustrations

1. Defective stock written off in books and allowed as deduction in early years is now sold for Rs. 10,000. The sales proceeds of the stock Rs 10,000 will be taxable u/s 41(1) even though the business is not in existence.
2. A has converted his business into a company, the company received the sales proceeds of the defective stock, the company being the successor in business will be liable in respect of that income.

b. Receipts from depreciable asset –Sec 41(2)

Where any depreciable asset being building, machinery, plant or furniture is owned by the assessee , who uses the same for the purposes of business and in respect of which depreciation is claimed u/s 32(1)(i), is sold, discarded, demolished or destroyed

and the moneys payable in respect of such building, machinery, plant or furniture, as the case may be, together with the amount of scrap value, if any, exceeds the written down value thereof, so much of the excess as does not exceed the difference between the actual cost and the written down value shall be chargeable to income-tax as income of the business of the previous year in which the moneys payable for the building, machinery, plant or furniture became due.

Example

A printer costing Rs 15,000, on which depreciation of Rs 8,000 was allowed, is sold for Rs.10,000, then the scrap value received on sale of printer Rs 3,000 after adjusting the WDV will be chargeable to tax as business income. In case of the printer forming part of block, it will be taxable as STCG. .

c. Scientific Research Asset—Sec 41(3)

Where an assessee claims and gets deduction u/s 35 (1) (iv) or 35 (2B) in respect of any capital asset used for scientific research and subsequently sells the asset without having been used for other purposes, then the excess of sale proceeds together with any amount of insurance claim and the amount allowed as deduction, which is in excess of the actual cost of the asset shall be chargeable as the income of the business or profession of the previous year in which the sale took place.

"Sold" includes a transfer by way of exchange or a compulsory acquisition under any law for the time being in force but does not include a transfer, in a scheme of amalgamation, of any asset by the amalgamating company to the amalgamated company, where the amalgamated company is an Indian company.

Illustration

A machine costing Rs 60,000 fully allowed as deduction u/s 35 in the earlier years, has been sold for Rs 20,000 in F.Y.2017-18, Rs. 40,000 will be the business income of the A.Y. 2018-19

d. Recovery of Bad debts —Sec 41(4)

Amount of any debt or part of debt allowed as bad debt u/s 36 (1) vii) and recovered in subsequent years shall be deemed to be profits and gains of business or profession in the year in which it is recovered.

e. Reserve for bad debts —Sec 41(4A)

Any amount withdrawn from the special reserve for bad debts by banking companies allowed as a deduction u/s 36 (1) (viii) shall be deemed to be the profits and gains of business or profession

and accordingly be chargeable as the income of the previous year in which such amount is withdrawn notwithstanding that the business or profession is no longer in existence in that year.

However, any loss, (except speculation loss) arising in the previous year in which such business or profession ceased to exist, and which could not be set off against any other income of that previous year will be set off against the income chargeable to tax under this section as aforesaid.

8. MISCELLANEOUS PROVISIONS

1. Prospecting etc., for mineral oil-sec-42.

As per Section 42 that in addition to the normal expenses, following expenses will be allowed in computing the profits or gains of any business of the prospecting for or extraction or production of mineral oils including petroleum or natural gas under agreement between the central government and the assessee :-

(a) expenditure by way of infructuous or abortive exploration expenses in respect of any area surrendered prior to the beginning of commercial production by the assessee;

(b) after the beginning of commercial production, to expenditure incurred by the assessee, whether before or after such commercial production, in respect of drilling or exploration activities or services or in respect of physical assets used in that connection,

(c) the depletion of mineral oil in the mining area in respect of the assessment year relevant to the previous year in which commercial production is begun and for such succeeding year or years as may be specified in the agreement.

If the assessee transfers the business wholly or in part or any interest therein as per the agreement, the unallowed expenditure as reduced by the proceeds of the transfer so far as they consist of capital sums, shall be allowed in the previous year of the transfer of the business or interest therein the surplus, if any, arising as result of such transfer shall be chargeable as the income of that year even if the business is no longer in existence in that year. The provision of the section will be applicable to the amalgamated or the resulting company in case of amalgamation or demerger of the assessee or its business.

2. Definitions of some relevant terms- Sec 43

Section 43 defines the meaning of certain terms used in sections 28 to 41 unless the context requires otherwise as under. These definitions have been dealt with at their appropriate places.

3. Changes in rate of exchange of currency-Section-43

In case of any increase or reduction in the liability as result of change in exchange rate of Indian rupee at the time of payment at new rate, the same will be adjusted in((by increasing/ decreasing) the cost /liability due. the cost and liability) due.

Such adjusted cost will be reckoned for the purposes of computing actual cost or expenditure on scientific research u/s 35 or 35A or u/s 36(1) (ix) or cost of acquisition of a capital asset u/s 50.

No adjustment will be made when the whole or any part of the liability is met, not by the assessee, but, directly or indirectly, by any other person or authority.

Any exchange rate under a future contract under FEMA to provide with a specified sum in a foreign currency on or after a stipulated future date at the rate of exchange specified in the contract to enable him to meet the whole or any part of the liability aforesaid, the amount, will also be adjusted accordingly.

4. Cost of acquisition of certain assets Sec 43C

Amalgamation

3.1. Where an asset other than the asset defined u/s 45(2), becomes the property of an amalgamated company, and

- the amalgamated company sells the asset as its stock-in-trade of the business carried on by it,
- then the cost of acquisition of the said asset to the amalgamated company in computing the profits and gains from the sale of such asset shall be –
- the cost of acquisition of the said asset to the amalgamating company,
- as increased by the cost, if any, of any improvement made thereto, and the expenditure, if any, incurred, wholly and exclusively in connection with such transfer by the amalgamating company.

Partition, gift, will etc.

3.2. where an asset becomes the property of the assessee on the total or partial partition of a Hindu undivided family or under a gift or will or an irrevocable trust, and the same is sold by the assessee as stock-in-trade of the business carried on by him,

- then the cost of acquisition of the said asset to the assessee in computing the profits and gains from the sale of such asset shall be the cost of acquisition

of the said asset to the transferor or the donor, as increased by the cost, if any, of any improvement made thereto, and the expenditure, if any, incurred, wholly and exclusively in connection with such transfer (by way of effecting the partition, acceptance of the gift, obtaining probate in respect of the will or the creation of the trust), including the payment of gift-tax, if any, incurred by the transferor or the donor, as the case may be.

5. Consideration for transfer of assets other than capital assets -Section 43A

Section 43 A extends the provisions of Section 50C/50CA to business assets and accordingly, the consideration received or accruing as a result of the transfer by an assessee of an asset (other than a capital asset), being land or building or both, is less than the stamp duty value adopted, assessed or assessable stamp duty authorities for levy of stamp duty on such transfer, then the stamp duty value shall be deemed to be the full value of the consideration received or accruing as a result of such transfer.

Where the date of agreement fixing the value of consideration for transfer of the asset and the date of registration of such transfer of asset are not the same, the value may be taken as the stamp duty value assessable on the date of the agreement, only if the amount of consideration or a part thereof has been received by any mode other than cash on or before the date of agreement for transfer of the asset.

6. Income of public financial institutions etc.- S. 43D

Income by way of interest in relation to such categories of bad or doubtful debts in case of a public financial institution or a scheduled bank or a State financial corporation or a State industrial investment corporation, or a public company, whose main object is carrying on the business of providing long-term finance for construction or purchase of houses in India for residential purposes shall be chargeable to tax in the previous year in which it is credited by the as per the guidelines issued by the Reserve Bank of India or the National Housing Bank in relation to such debts, or which is actually received by that institution or bank or corporation or company, whichever is earlier.

7. Insurance business-Section-44.

Profits and gains of any business of insurance, including any such business carried on by a mutual insurance company or by a co-operative society, shall be computed in accordance with the rules contained in the First Schedule overriding the normal provisions of the Act for computation of income under different heads of income.

8. Trade, professional or other association- S. 44A

Sec 44A deals with certain trade, professional or similar association formed solely for the purposes of protection or advancement of the common interests of their members and 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.

When the receipts of such associations by way of subscription or otherwise falls short of the expenditure , not being capital expenditure, incurred by such association during that previous year, such deficiency shall be allowed to deducted from its normal income, of that association under the head "Profits and gains of business or profession and if there is no income assessable under that head or the deficiency allowable exceeds such income, the whole or the balance of the deficiency, shall be allowed as a deduction in under any other head while computing the income of the association .

The amount of deficiency to be allowed as a deduction under this section shall in no case exceed one-half of the total income of the association. In computing the income of the association for the relevant assessment year, effect shall first be given to any other provision of this Act under which any allowance or loss in respect of any earlier assessment year is carried forward and set off against the income for the relevant assessment year.

9. Compulsory maintenance of accounts –Sec 44AA

U/s 44AA it is mandatory for the following persons to keep and 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 this Act :-

(a) Every person who carries on legal, medical, engineering or architectural profession or the profession of accountancy or technical consultancy or interior decoration or any other notified profession,

(b) Every person who carries on business or profession other than the above professions , whose income from business or profession exceeds Rs 1,20,000 or s total sales, turnover or gross receipts, in business or profession exceeds Rs 10 lakh in any one of the three years immediately preceding the previous year in case of an existing business or profession.

(c) Every person , in case of a business or profession newly set up in any previous year, if his income from business or profession is likely to exceed Rs 1,20,000 or his total sales, turnover or gross receipts, in business or profession are or is likely to exceed Rs 10 lakh during such previous year;

(d) Every assessee, who has claimed his income to be lower than the profits or gains of his business during a previous year than the prescribed presumptive income under sections 44 AE, 44BB or 44BBB.

(e) Every person, who has claimed his income to be lower than the deemed presumptive income u/s 44AD and his income exceeds the maximum amount which is not chargeable to income-tax during such previous year.

Other Points

(i) The Board may, having regard to the nature of the business or profession carried on by any class of persons, prescribe, by rules, the books of account and other documents (including inventories, wherever necessary) to be kept and maintained, the particulars to be contained therein and the form and the manner in which and the place at which they shall be kept and maintained.

(ii) The Board may prescribe, by rules, the period for which the books of account and other documents to be kept and maintained shall be retained.

10. Compulsory Audit of accounts - Section 44AB.

U/s 44AB, every person carrying on -

a) business shall, if his total sales, turnover or gross receipts, in business exceed or exceeds Rs. two crore in any previous year; or

(b) profession shall, if his gross receipts in profession exceeds Rs 50 lakh in any previous year; or

(c) carrying on the business shall, if the profits and gains from the business are deemed to be the profits and gains of such person u/s 44AE, 44BB, OR 44BBB and he has claimed his income to be lower than the profits or gains so deemed to be the profits and gains of his business, as the case may be, in any previous year; or

(d) the *business* shall, if the profits and gains from the *business* are deemed to be the profits and gains of such person u/s 44AD and he has claimed such income to be lower than the profits and gains so deemed to be the profits and gains of his *business* and his income exceeds the maximum amount which is not chargeable to income-tax in any *previous year* get his accounts of such previous year audited by an accountant before the specified date for furnishing the return of income u/s 139(1) and furnish by that date 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

This section does not apply to a person, who derives income of the nature referred to in Sec. 44B or Sec 44BBA.

In a case where such person is required by or under any other law to get his accounts audited, it shall be sufficient

compliance with the provisions of this section if such person gets the accounts of such business or profession audited under such law before the specified date and furnishes by that date the report of the audit as required under such other law and a further report by an accountant in the form prescribed under this section.

9. PRESUMPTIVE INCOME

A. Profits and gains of business - Section 44AD

U/s 44AD, a new presumptive income has been devised for small eligible assessees having turnover of less than Rs 2 Crore from and eligible business. As per the sachem in case of :-

- (a) Any **Eligible Assessee being** an individual, Hindu undivided family or a partnership firm, who is a resident, but not a limited liability partnership firm (LLP) ,
- (b) who is engaged in an **eligible business** being a business any business except the business of plying, hiring or leasing goods carriages(Sec 44AE) ; and
- (c) whose total turnover or gross receipts in the previous year does not exceed an amount does not exceed an amount of two crore rupees, and
- (d) who has not claimed deduction u/s 10 , 10AA .10B or 10BA or deduction under any provisions of Chapter VIA under the heading "*C. - Deductions in respect of certain incomes*" in the relevant assessment year; the following sum shall be **deemed** to be the **profits** and gains of such business chargeable to tax:-
 - **8%** of gross receipts or total turnover or
 - **6%** of the turnover or gross receipts which is received by an account payee cheque/ bank draft / use of electronic clearing system through a bank account ;

during the previous year or before the due date of filing return u/s 139(1) in respect of that previous year , **or**

a sum higher than the aforesaid sum claimed to have been earned by the eligible assessee.

Other points

- (a) Any deduction in respect of expense (including depreciation, remuneration and interest payable to partners) allowable under the provisions of sections 30 to 38 shall be deemed to have been already given full effect to and no further deduction under those sections shall be allowed.
- (b) The written down value of any asset of an eligible business shall be deemed to have been calculated as if the eligible

assessee had claimed and had been actually allowed the deduction in respect of the depreciation for each of the relevant assessment years

(c) This provision will not apply to

- (i) a person carrying on profession specified in S. 44AA such as doctor, architect, lawyer, CA, engineer etc.;
- (ii) a person earning income in the nature of commission or brokerage; or
- (iii) a person carrying on any agency business.

(d) Such assessee has to opt for the scheme of presumptive tax u/s 44AD, for five consequent years,

(e) If the assessee does not opt for the scheme, during the five assessment years, he cannot again opt for the scheme for next five years from that year.

(f) The eligible assessee is to pay advance tax by 15th March of the financial year.

(g) An eligible assessee who has opted for the scheme shall not be liable for compliance of the provisions of Section 44AA and 44AB in respect of maintenances and audit of account etc.

(h) An eligible assessee may claim his profits to be lower than 6%/8% and whose total income is above the taxable limit. Such assessee shall be liable to comply with the provisions of Section 44AA and 44AB in respect of maintenances of books and other documents and audit of account and submission thereof. .

Illustration :

1. Ashok (an eligible assessee) has turnover of an eligible business is 150 lakh for A.Y 2017-18 and Rs 180 lakh respectively for A.Y. 2018-19. Profit of the business u/s 44AD will be assumed to be 8% i.e. Rs 12 lakh and Rs 14.40 lakh respectively. All the expenses will be deemed have been allowed.
2. For the A.Y. 2019-20, Ashok does not opt for the scheme u/s 44AD (1) for five consecutive assessment years, he will not be eligible to again opt for it for next five assessment years succeeding A.Y.2019-20 i.e., from A.Y. 2020-21 to 2024-25.

B. Profits and gains of profession Section 44AD

U/s 44ADA, In case of **an eligible Assessee**

- (a) who is engaged in any profession referred to in section 44AA(1) such as legal, medical, engineering or architectural profession or the profession of accountancy or technical

consultancy or interior decoration or any other notified profession and ,

- (b) whose total gross receipts does not exceed **50 lakh rupees** in a previous year,

deemed Income will be **50% of the total gross receipts**, or any higher Income claimed by the assessee.

In case of a less income the assessee will have to have his accounts audited. Such an assessee will have to pay advance tax by 15 March and all expenses will be deemed to have been allowed. Provisions relating to declaring lower income and other matters I be applicable under this section also.

C. Plying, hiring/ leasing goods carriages-S.44AE

U/s 44AE, in case of an assessee, who

- (a) owns **not more than ten goods carriages** at any time during the previous year and
- (b) who is engaged in the business of plying, hiring or leasing such goods carriages, the income of such business chargeable to tax under the head "Profits and gains of business or profession" shall be deemed to be the aggregate of the profits and gains, from all the goods carriages owned by him in the previous year, computed at **Rs 7,500 per month** or part of a month during which the goods carriage is owned by the assessee in the previous year or an amount claimed to have been actually earned from the vehicle, whichever is higher.

All other provisions like declaring low income or loss, no all expense including depreciation, remuneration etc. deemed as allowed, are applicable under this section also. Further the section applies on hired goods carriages also.

D. Shipping business of non-resident- Sec.44B.

In the case of an assessee, being a non-resident, engaged in the business of operation of ships, a sum equal to **7.5%** of the aggregate of the amounts paid or payable (whether in or out of India) to the assessee or to any person on his behalf on account of the carriage of passengers, livestock, mail or goods shipped at any port in India; and the amount received or deemed to be received in India by or on behalf of the assessee on account of the carriage of passengers, livestock, mail or goods shipped at any port outside India including amount received by way of demurrage charges or handling charges or any other amount of similar nature shall be deemed to be the profits and gains of such business chargeable to tax under the head "Profits and gains of business or profession".

E. Exploration, etc., of mineral oils- Sec 44BB.

Sec.44BB, applies to a non-resident assessee who is engaged in the business of providing services or facilities in connection with, or supplying plant and machinery including ships, aircraft, vehicles, drilling units, scientific apparatus and equipment, used for the purposes of the said business; on hire used, or to be used, in the prospecting for, or extraction or production of, mineral oils, In such cases presumed income shall be 10% of the aggregate of;

- the amounts paid or payable (whether in or out of India) to the assessee or to any person on his behalf on account of the provision of services and facilities in connection with, or supply of plant and machinery on hire used, or to be used, in the prospecting for, or extraction or production of, mineral oils including petroleum and natural gas in India; and
- the amount received or deemed to be received in India by or on behalf of the assessee on account of the provision of services and facilities in connection with, or supply of plant and machinery on hire used, or to be used, in the prospecting for, or extraction or production of, mineral oils outside India shall be deemed to be the profits and gains of such business chargeable to tax under the head "Profits and gains of business or profession except in a case where the provisions of Sec 42, 44D, 44DA, 115A or 293A are applicable for the purposes of computing profits or gains or any other income.
- An assessee may claim lower income than 10%, if he keeps and maintains such books of account and other documents as required u/s 44AA and gets the accounts audited and furnishes a report of such audit u/s 44AB and thereupon, the Assessing Officer shall proceed to make an assessment of the total income or loss of the assessee u/s 143(3) and determine the sum payable by, or refundable to, the assessee.

F. Operation of aircraft of non-residents- S. 44BB

Section 44BB A provides that in the case of an assessee, being a non-resident, engaged in the business of operation of aircraft, a sum equal to 5% of aggregate of the amounts the amount paid or payable (whether in or out of India) to the assessee or to any person on his behalf on account of the carriage of passengers, livestock, mail or goods from any place in India; and the amount received or deemed to be received in India by or on behalf of the assessee on account of the carriage of passengers, livestock, mail or goods from any place outside India shall be deemed to be the profits and gains of such business chargeable to tax under the head "Profits and gains of business or profession".

G. Foreign companies engaged civil construction, turnkey power projects etc.- Sec44BBB.

U/s 44BBB, a sum equal to 10% the amount paid or payable, whether in or out of India to an assessee, being a foreign company, engaged in the business of civil construction or the business of erection of plant or machinery or testing or commissioning thereof, shall be deemed to be the profits and gains of such business chargeable to tax .

The assessee is at liberty to declare a lower income by maintaining accounts and other documents u/s 44AA and getting the same audited u/s 44AB and submitting the audit report in prescribed form and thereupon, the Assessing Officer shall proceed to make an assessment of the total income or loss of the assessee u/s 143 (3) and determine the sum payable by, or refundable to, the assessee.

H. Head office expenditure - non-residents-S.44C

Section 44C provides that deduction in respect of the expenditure in the nature of head office expenditure incurred by a non-resident assessee shall not exceed 5% of the adjusted total income; or the amount of head office expenditure as is attributable to the business or profession of the assessee in India, whichever is less. In case of loss, the deduction shall be computed @ 5% of the average adjusted total income of the assessee.

▪ "Adjusted total income" means the total income computed without giving effect to the allowance u/s 32,32A 33,33A ,36(1)(ix) , any loss carried forward u/s 72(1) , 73(2) ,74(3) or 74A(3) or the deductions under Chapter VI-A;

▪ "Average adjusted total income" means one third of the aggregate adjusted total income of last three years or one half of the aggregate adjusted total income of last two years or , the amount of the adjusted total income in respect of the previous year relevant to that assessment year , as the case may be depending upon the number of year the assessee has been assessed in India

▪ "head office expenditure" means executive and general administration expenditure incurred by the assessee outside India, including expenditure incurred in respect of

(a) rent, rates, taxes, repairs or insurance of any premises outside India used for the purposes of the business or profession;

(b) salary, wages, annuity, pension, fees, bonus, commission, gratuity, perquisites or profits in lieu of or in addition to salary, whether paid or allowed to any employee or other person employed in, or managing the affairs of, any office outside India;

(c) travelling by any employee or other person employed in, or managing the affairs of, any office outside India; and

(d) such other matters connected with executive and general administration as may be prescribed.

I. Royalties, etc., in case of non-residents-Sec44DA

U/s 44DA the income of non-residents or foreign companies in receipt of income by way of royalty or fees for technical services from Government or an Indian concern under an agreement with them and such non-resident carries on business or performs professional services in India through a permanent establishment or from a fixed place of profession situated therein, shall be computed under the head "Profits and gains of business or profession". No deduction shall be allowed, in respect of —

- (i) any expenditure or allowance which is not wholly and exclusively incurred for the business of such permanent establishment or fixed place of profession in India; or
- (ii) any amounts, (otherwise than towards reimbursement of actual expenses) by the permanent establishment to its head office or to any of its other offices :

Every such non-resident (not being a company) or a foreign company shall keep and maintain books of account and other documents in accordance with the provisions contained in Sec 44 AA get his accounts audited and furnish along with the return of income, the report of such audit in the prescribed form.

J. Reorganization of co-operative banks- Sec. 44DB

Section 44DB (1) deals with reorganization of co-operative banks due to amalgamation or demerger etc. The section provides for pro rata deduction u/s 32, 35D, 35DD or 35DDA to the predecessor bank in the ratio of number of days upto the date of reorganisation and correspondingly, the amount of deduction allowable to the successor co-operative bank 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 the total number of days in the financial year, in which the business reorganisation has taken place.

Illustration

Total amount of deduction allowable to a Bank under different sections works out to Rs 50,000. Reorganization of a bank takes place on 01/09/2016. The deduction will be allowed to the predecessor bank and the resultant bank pro rata for 153 days (from 01-04-2016 to 31-08-2016 and 212 days i.e. from 01-09-2016 to 31-03-2017 respectively).

The predecessor bank will be able to deduct Rs 20,959 being $\text{Rs } 50,000 \times 153/365$ and the resulting bank will get Rs 29,041 i.e. $50,000 \times 212/365$.

This is subject to some conditions namely :-

- (i) all the assets and liabilities of the undertaking or undertakings immediately before the transfer become the assets and liabilities of the resulting co-operative bank;
- (ii) the assets and the liabilities are transferred to the resulting co-operative bank at values (other than change in the value of assets consequent to their revaluation) appearing in its books of account immediately before the transfer;
- (iii) the resulting co-operative bank issues, in consideration of the transfer, its membership to the members of the demerged co-operative bank on a proportionate basis;
- (iv) the shareholders holding 75% or more in value of the shares in the demerged co-operative bank (other than shares already held by the resulting bank or its nominee or its subsidiary immediately before the transfer), become shareholders of the resulting co-operative bank, otherwise than as a result of the acquisition of the assets of the demerged co-operative bank or any undertaking thereof by the resulting co-operative bank;
- (v) the transfer of the undertaking is on a going concern basis; and
- (vi) the transfer is in accordance with the conditions specified by the Central Government, by notification in the Official Gazette, having regard to the necessity to ensure that the transfer is for genuine business purposes.

10. ILLUSTRATIONS:

Illustration -35

From the following Income & Expenditure account of Law Bros. for the year ending March 31, 2018, compute the total income of the firm.

To Expenses	150,000	Professional Receipts	480,000
To Depreciation	20,000		
To Remuneration to partners	250,000	By Other fees	90,000
Interest on Capital to partners @ 20 per cent	20,000		
To Net Profit	130000		
Total	570000		570000

Other Information:

1. Expenses include Rs. 18,000 and Rs. 12,000 paid in cash as brokerage to a single party on a single day.
2. Depreciation calculated as per section 32 is Rs. 40,000

SolutionComputation of Total Income of Law Bros. (A. Y. 2016-17)

Net profit as per Income & Exp account	1,30,000
Add: Expenses not allowable	
40A(3)- Cash paid to broker over Rs. 10,000	30,000
40(5) Excess interest to partners -20,000 *8/20	8,000
	1,68,000
Less: Depreciation u/s32 (40,000-20,000)	20,000
	1,48,000
Add: Remuneration to partners debited in PLA	2,50,000
Book Profits before remuneration	3,98,000
Remuneration to partners Actual Rs 2,50,000 or 1.50.000 +60% of Rs 398200-150000) = 2,98,920	2,98,920
Total Income	99,080

Illustration -36

From the given Trading and P & L A/c of A&B for the year ended 31st March 2018 , compute taxable income of the firm for the A. Y. 2018-19

Particulars	Rs.	Particulars	Rs.
To Opening Stock	75,000	By Sales	20,00,000
To Purchases	15,00,000	By Closing Stock	85,000
To Gross Profit	<u>5,10,000</u>		
Total	<u>20,85,000</u>	Total	<u>20,85,000</u>
To Salaries	2,50,000	By Gross Profit	5,10,000
To Sales Commission	40,000	By Bad Debts Recovery	25,000
To Sales Tax	35,000		
To General Expenses	5,000		
Advance Income Tax	54,000		
To Interest on Loan	42,000		
To Interest on Capital	18,000		

To Depreciation on Furniture & Fittings	4,000		
To Advertisement	16,000		
To Free Distribution of Samples	3,000		
To Insurance premium on Life of Partners	8,500		
To Printing & Stationery	3,500		
To Net Profit	56,000		
Total	5,35,000	Total	5,35,000

Additional information:

- Salaries include Rs. 40,000/- paid to partners, as per partnership deed and well within the limits u/s 40(b).
- General Expenses are incurred for the purposes of pleasure tour of partners with their family members to Goa.
- Income Tax includes Rs. 14,000 paid for the partners.
- Bad Debts recovered were earlier allowed as a deduction.
- Interest on Capital to partners is in excess of limits specified u/s 40(b) by Rs. 1,500/- but as per partnership deed.
- Cash expenses over Rs 35,000 for carriage of Rs. 40,000.

SOLUTION:

Computation of Total Income of X & Y Co. for A.Y. 2018-19		
Particulars	Rs.	Rs.
Profit as per Profit and Loss Account		56000
Add: Exp. disallowed /considered separately		
Salaries to Partners	40000	
General Expenses incurred for personal purpose by the partners	5000	
Cash expenses 40A(3)	40000	
Income Tax (Advance)	54000	
Interest on Capital	18000	
Insurance on Life of Partners	8500	165500
		221500
Less: Interest to partners (18000-1500)		16500
Book Profit		205000
Less: Salaries to partners		40000
Business income		165000

7. SELF-EXAMINATION QUESTIONS:

- 1) Define and explain the term "Business".
- 2) Explain any six deductions which are specifically allowed as a deduction while computing income from business or profession.
- 3) Give a detailed note on depreciation
- 4) Is Depreciation always allowed on Written down Value?
- 5) What happens, when block ceases to exist?
- 6) Discuss the tax treatment when block comes to zero.
- 7) What are the incomes chargeable under the head "Profits and Gains of Business or Profession"?
- 8) Explain the items of expenses, which are expressly not allowed as deductions while computing income from "Profits and Gains of Business.
- 9) Explain "while computing Profits and Gains of Business or Profession" "Section 37(1) is the residuary section to claim deduction.
- 10) Explain expenses allowed on payment basis U/s 43B.
- 11) State the disallowance under Section 40A (3) if a purchase bill of Rs 45,000 was immediately paid by cash. (*Ans: Rs. 45,000*)
- 12) State whether following expenses are allowed as a deduction or not while computing income from business or profession, if not, give reasons:
 - a. Interest paid outside India wherefrom no tax has been deducted nor there is any representative assessee.
 - b. Income tax paid by the firm.
 - c. Salary paid outside India wherefrom no tax has been deducted nor there is any representative assessee.
 - d. Salary paid to a partner.
 - e. Guest House expenses.
 - f. Advertisement expenses.
 - g. Contribution to Gratuity Fund.
 - h. Interest on borrowed capital.

(*Ans: Item f & h only allowable, d allowed subject to book profits*)
- 13) Discuss the admissibility and/ or inadmissibility of the following expenditure under the Provision of Income Tax Act, 1961

- a. A technical consultant was paid consultancy fee of Rs. 20,000 in cash by assessee and a deduction was claimed towards the expenditure.
- b. A senior advocate conducted the Income tax proceeding before the Income Tax authority and was paid Rs 18,000.
- c. Provision made for gratuity as per actuary valuation of Rs 1,00,000.
- d. A sum of Rs 1,30,000, was paid towards sales tax liability in the account for the year ending 31.3.2016
- e. Stock-in-trade was lost to fire amounting to Rs 10,000/- and was debited to Profit and Loss Account. (Ans : a, b & e allowable)
- f. Discuss the implication of the following transactions in the case of a doctor running a nursing home:
- g. Amounts received from the employees of the nursing home as contribution towards Provident Fund for the month of March 2018 paid to the PF - Rs 25,000 in December 2018
- h. Cash paid for purchase of medicines –Rs 50,000

(Ans. 25000 Income u/s/ 43 B (2) Rs 50,000 disallowed u/s 40A (3))

- i. Are the following expenses allowable as deduction under section 37(1): (a) Litigation expenses for official purposes? (b) Expenses relating to purchase of stationary for official purpose and (c) interest on loan taken for the purpose of paying income-tax. (Ans; 1&2 allowable)

14) From the P/L A/c of X for the year ending 31-03-2018, ascertain total income for the assessment year 2018-19 :

Expenses	Rs.	Income	Rs.
General expenses	13,400	Gross profits	3,64,500
Bad debts	22,000	Commission	8,600
Advance tax	21,000	Brokerage	37,000
Insurance	600	Sundry receipts	2,500
Salary to staff	26,000		
Salary to X	32,000		
Interest on overdraft	4,000		
Interest on loan to Mrs. X	42,000		
Interest on capital of X	23,000		
Depreciation	48,000		
Advertisement exp.	7,000		
Contribution to RPF	13,000		
Net profit	1,60,600		
Total	4,12,600	Total	4,12,600

Other information:

(A) Depreciation allowable is Rs. 37,300 as per the I.T. Rules.

(B) Gen. exp. include Rs. 500 for arranging a party to a friend

(Ans $160600+21000+32000+23000+48000-37300+500 = 247800$)

15) From the following data, calculate the depreciation admissible to an individual carrying on business, for A.Y. 2018-19

16)

Particulars	%	WDV
Factory Building	10	5,00,000
Plant & Machinery	20	8,00,000
Addition to Plant		1,00,000
Sale proceeds of Plant (cost 1 lakh)		5,00,000
Furniture & Fixtures	10	1,00,000
Motor Car	20	60,000
New computer	60	60,000

(buildg. Rs. 50,000, P&M . 60,000, Comp. Rs.36000, Furni. Rs.10,000 & Car Rs.12,000)

17) From the following, ascertain depreciation admissible and other liabilities, if any. In respect of the previous year relevant to the AY 2018-19.

Particulars	Plant & Mach	Building
Rate of Depreciation	25%	10%
WDV at the beginning of the year	Rs2,50,000	Rs 5,00,000
Additions during the year	Rs 3,00,000	Nil
Sales during the year	Rs10,00,000	Rs 2,00,000

(Ans. P&M Rs. Nil Rs. 2,00,000 Short term capital gain, Building Rs. 5,000)

18) X Ltd. owns two plants A & B on 1/4/ 2017 (depreciation-15% per cent) with opening depreciated value of the block Rs. 2,37,000. It purchases Plant C with depreciation -15% on 31/5/ 2017 for Rs. 20,000 and sells Plant A on 10/04/2017 for Rs 10,000, Plant B on 12/12/2017 for Rs. 15,000 and Plant C on 1/03/2018 for Rs. 24,000. Determine the WDV of the block as on 31/03/2014 and also the depreciation

(Ans. $237000+20000-49000 = 208000$ Short Term Capital Loss, block empty, Depn -NIL))

19) Compute depreciation for A.Y. 2018-19 from the following:

Plant & Machinery A, B & C – WDV on 1/4/ 2017 Rs. 5,00,000 rate of dep.15%. Plant D purchased on 12/06/2017 Rate of dep. 15% for Rs. 40,000. Plant A sold on 8/12/ 2017 for Rs. 1,60,000

(Ans Value of Block $500000+40000- 160000 = 380000$ Dep. 57000)



CAPITAL GAINS

Sections 45 to 55

Synopsis:

1. Introduction and Objectives
2. Basis of charge S.45, 46A
3. Capital asset – S. 2(14)
4. Types of assets – Short Term & Long Term
5. Transfer –S.2(47)
6. Types of Capital Gains - S 2(29A/B)/(42A/B)
7. Period of holding
8. Computation of Capital Gains
9. Value of Consideration
10. Cost of Transfer
11. Cost of Acquisition
12. Fair Market Value
13. Transactions covered u/s 49(1)
14. Cost of improvement
15. Indexed cost of acquisition /improvement
16. Transactions not regarded as transfer
17. Typical Illustrations
18. Self Assessment Questions

1. INTRODUCTION AND OBJECTIVES

The Income tax was introduced as a tax on income. Income by definition excludes capital receipts. Hence, levying tax on capital gains arising on transfer of capital assets was not a popular idea. Further, capital assets are acquired out of the income on which income tax has already been paid. Moreover, capital gain is not an income *per se* but only reflects the inflated value of the asset over a period of years due to reduction in purchasing power of money because of inflation.

However, a progressive tax regime could not ignore capital gain as a precious source of revenue. The result is a complex cobweb of legal provisions seeking to tax capital gains.

The lesson intends to explain different aspects of tax treatment of the capital gains including the concept of “Capital Asset”, “Transfer”, what constitutes a capital asset and what is not capital asset, types of capital gains, concept of indexation and computation of the capital gain and other machinery provisions dealing with contained in sections 45 to 55.

2. BASIS OF CHARGE -SEC. 45/46A

2.1 Capital Gains Defined :

Section 45 is the charging section. It states, *“any profits or gains arising from the transfer of a capital asset effected in the previous year shall be the income of the previous year in which the transfer took place”*

Section 45 is attracted on loss or profit arising on ‘transfer’ of a ‘capital Asset’ during the ‘previous year’. Hence, the section will apply if:-

- (i) a capital asset ,
- (ii) is transferred by the assessee,
- (iii) during the previous year and
- (iv) it results in some gain or loss.

Section 2(14) defines “capital asset” and section 2(47) defines “transfer”. On a plain reading of the sections, it would appear that every asset may not be a ‘capital asset’ nor every movement of a capital asset from one person to another can be called “transfer”. If the two ingredients do not co-exist simultaneously, there will be no liability for tax u/s 45.

E.g., profit on transfer of a personal motorcar will not be chargeable as capital gain because motorcar being a personal effect is not a ‘capital asset’.

Similarly, where the shares are registered in the name of a legal heir on the death of a shareholder, there will not be any capital gain as devolution or transmission of an asset unto heirs by succession is not regarded as transfer u/s 2(47).

2.2 Other receipts chargeable to capital tax

Sec. 45 extends the term “capital gain” to cover several other receipts, discussed below:-

a) Insurance money

Money or other assets received during the previous year from an insurer on account of damage to or destruction of a capital asset, as a result of:

- I. Flood, typhoon, hurricane, cyclone, earthquake or other convulsions of nature, or
- II. Riot or civil disturbance, or
- III. Accidental fire or explosion, or
- IV. Action by an enemy or action taken in combating an enemy

b) Conversion of capital asset into stock

Transfer by way of conversion, by the owner of a capital asset into, or its treatment by him as stock-in-trade of a business carried on by him but is chargeable to tax in the previous year in which such stock-in-trade is sold or otherwise transferred by him.

c) Interest in securities

Transfer made by a depository or a participant of beneficial interest in any securities during the previous year in which such transfer takes place.

d) Transfer of asset as capital to firm , AOP or BOI

Transfer of a capital asset made by a person to a firm or other association of persons or body of individual (not being a company or a co-operative society) in which he is or becomes a partner or member by way of capital contribution or otherwise in the previous year , in which the transfer takes place.

e) Transfer of asset on dissolution of firm , AOP or BOI

Transfer of a capital asset by way of distribution of capital assets on dissolution of a firm or association of persons or body of individuals (not being a company or co-operative society) or otherwise, in the previous year in which the transfer takes place.

f) Compulsory Acquisition

Transfer of capital asset by way of compulsory acquisition under any law is chargeable to tax in the previous year in which such compensation or part thereof is received.

Any additional compensation shall be taxable in the previous year, in which it is actually received.

If any court, tribunal or any authority subsequently reduces the initial compensation, the capital gains assessed in the year of receipt of initial compensation or enhanced compensation will be amended to re-compute the capital gains with reference to such reduced compensation.

g) Repurchase of Units of Mutual Funds

Transfer of capital asset being the units of UTI or other mutual funds issued under the Equity-Linked Savings Scheme on the repurchase thereof by the mutual fund will be taxed in the year of such repurchase.

h) ESOP /ESOS

Sale value of the shares issued to employees under an equity stock option plan/scheme as reduced by the cost of acquisition / indexed cost of acquisition of the shares will be taxed in the year of such issue.

i) Buyback- Sec.-46A

The value of a consideration received by the shareholder from a company under a scheme to buyback its own shares u/s 77A of the Companies Act, 1956 as reduced by the cost of acquisition /indexed cost of acquisition will be taxed in the year of buyback.

j) Joint Development Agreement(JDA)-Sec.- 45(5A)

The value of the capital asset (Land or building or both) transferred (by an individual or a HUF) under a registered specified agreement called Joint Development Agreement (JDA) to develop real estate for a consideration of a share being land and building or both, whether with or without or part payment of consideration in cash shall be the stamp duty valuation on the date on which the competent authority issues a completion certificate for the entire property and capital gain will be chargeable accordingly on that date.

3. CAPITAL ASSET – S. 2(14)

Sec. 2(14) defines capital asset as:

“Property of any kind held by an assessee, whether or not connected with his business or profession,” but does not include -

- a. **any stock-in-trade, consumable stores or raw materials** held for the purposes of his business or profession ;
- b. **personal effects**, i. e. 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 -
 - (a) Jewellery; b) archaeological collections; (c) drawings; (d) paintings; (e) sculptures; or (f) any work of art.

For this purpose, “Jewellery” includes:

- (a) **ornaments made of gold, silver, platinum** or any other precious metal or any alloy containing one or more of such precious metals, whether or not containing any precious or

semi-precious stones, and whether or not worked or sewn into any wearing apparel;

(b) **precious or semi-precious stones**, whether or not set in any furniture, utensil or other article or worked or sewn into any wearing apparel;

Although jewellery is a movable property held, for personal use, it is deemed as a “capital asset”. Definition of jewellery covers only ornaments, not other articles like **silver or gold utensils, which are neither “jewellery nor ornaments”**.

c. **Agricultural land** in India, not being land situate in :

a. areas not in the jurisdiction of a municipality, municipal corporation notified area committee, town area committee, town committee, or by any other name or a cantonment board or cantonment board having population of 10000 or more and

b. in any area within the distance, measured aerially, from the local limits from any area of municipality etc. as above-

Distance not more than	Population of the area of municipality etc. as per last published census
2 KM	10,001 – 1,00,000
6 KM	1,00,001 – 10,00,000
8 KM	More than 10,00,000

d. Special Bearer Bonds, 1991

e. 6 1/2 per cent Gold Bonds, 1977

f. 7 per cent Gold Bonds, 1980

g. National Defence Gold Bonds 1980

h. Gold deposit Bonds under old Deposit Scheme 1999

The section clarifies *that* “property” shall include any rights in or in relation to an Indian company, including rights of management or control or any other rights whatsoever;

4. TRANSFER –S.2(47)

Sec 2(47) defines “Transfer” in an inclusive definition:

“Transfer in relation to capital assets includes the following:-

(1) sale, exchange or relinquishment of the asset ;

Relinquishment of a right means transfer of a right in favour of another person e.g. sale of right to subscribe shares;

(2) extinguishment of rights on the capital asset;

Extinguishment of rights results in cessation or destruction or cancellation of rights in a capital asset like surrender of tenancy right for e.g. buyback of shares results in extinguishment of shares;

(3) compulsory acquisition under any law;

- (4) conversion of capital asset into stock in trade of a business;
- (5) maturity or redemption of a zero coupon bond issued by an infrastructure capital company, a fund or a public sector company notified by the central government in respect of which, no payment or benefit is received before maturity or redemption;
- (6) any transfer involving the allowing the possession of an immovable property u/s 53A of Transfer of Property Act, in part performance of the contract for transfer of that property;
- (7) any transaction involving transfer of membership of a group, association housing society, company, etc., which have the effect of transferring or enabling enjoyment of any immovable property or any rights therein in any manner whatsoever;
- (8) distribution of assets on the dissolution of a firm, body of individuals or association of persons;
- (9) transfer of a capital asset by a partner or member to the firm or AOP, whether by way of capital contribution or otherwise;
- (10) transfer under a gift or an irrevocable trust of shares, debentures or warrants allotted by a company directly or indirectly to its employees under the ESOP Scheme of the company as per the guidelines of the Central Government.

Sections 47 and 47A list out many transactions, which are not regarded as “transfer” e.g. transfer upon reorganisation of business entitles like amalgamation, demerger, gift, will etc.

5. TYPES OF CAPITAL ASSETS

A capital asset may be classified as a short term capital asset or a long term capital asset depending upon the period for it held by the assessee before such asset is transferred that is:-

a) Short Term Capital Asset (STCA)- Sec 2(42A)

- Short-term capital asset means a capital asset held by an assessee for less than 36 months before it is transferred.
- The period of 36 months is taken as 12 months in the following cases:
 - (i) Equity or Preference shares whether quoted or not;
 - (ii) Securities like debentures, government securities and notified derivatives, which are listed in recognised stock exchange u/s 10-23(D);
 - (iii) Units of UTI;
 - (iv) Units of equity oriented Mutual Funds;
 - (v) Zero Coupon Bonds;
- In case of unlisted Shares, the period of holding is taken as 24 months.

- in case of immovable property, being land or building or both reduced from the existing 36 months to 24 months.
Hence period of holding is 12, 24 or 36 months depending upon the asset.

b) **Long Term Capital Asses (LTCA)**

A long term capital means a capital asset, which is not a short-term capital asset. In other words, a capital asset will be a long term asset if it is held for more than 12, 24 or 36 months before it is transferred.

6. TYPES OF CAPITAL GAINS

Capital gains arising on the transfer of a capital asset will short term capital gain or long term capital gain depending upon the type of the asset which is transferred that is:-

(i) **Short Term Capital Gain (STCG)**

Capital gain arising on transfer of a short term capital asset i.e. asset held by an assessee for less than 36/ 24/12 months will be short term capital gain and any loss arising on the transfer of short term asset will be short term capital loss – Section 2(29B)

Further, capital gains arising on sale of long term business assets in a block in case of a slump sale as covered under section 50 would be treated as a short term capital gain or short term capital loss.

(ii) **Long Term Capital Asses (LTCG)**

Long-term capital gain is the gain arising on transfer of a long-term asset or an asset held by an assessee for 36/12/24 months or more. Conversely, any loss arising on transfer of long-term asset will be long-term capital loss – Section 2(42B)

5. PERIOD OF HOLDING- S. 2(42A):

Holding of an asset is the yardstick to determine whether the type of capital gains arising on transfer of the capital asset. Some important principles to determine the holding of an asset are given as under:-

1. In case of shares held in company in liquidation, the period subsequent to the date of liquidation will not be included. Period of holding will stop running on date of liquidation.

Illustration-1

A company goes into for winding up on 01/01/2014. The liquidator settles the claim on 01/01/2018. In computing the period of holding, the period after 01/01/2014 will not be included.

2. In case capital assets have become the property of the assessee in circumstances mentioned in section 49(1) in determining the period, the period for which the previous owner held the capital asset will also be included.

Illustration- 2:

A dies on 01/01/2016 leaving his house, which was purchased on 15/02/2003 to his son B. B sells this house on 20/03/2018. The capital gain arising of the house will be long term as the holding of the house will be computed from the date of acquisition from 15/02/2003, date since which the previous owner A held the house.

3. In case of shares of an amalgamated company allotted to a shareholder against the shares in an Indian company, which was amalgamated, the period for which the assessee held the shares in the amalgamated company will also be included.

Illustration-3:

R purchased shares of S Ltd on 12/11/2010. S Ltd amalgamated with H Ltd. on 31/12/2017. Under the scheme of amalgamation, original 1000 shares in S Ltd were converted into 300 shares of H Ltd. R sells these 300 shares of H Ltd. on 01/01/2018. The capital gain will be treated as long term as the period of holding will be reckoned from 12/11/2010 and not 31/12/2017.

4. In case of *rights issue* of shares or other securities subscribed to by the assessee on the basis of his rights to subscribe, the counting of the period shall start from the date of allotment by such person or other person in whose favour such right has been renounced.
5. In case of *renunciation of a rights*, for the person who has acquired the rights, the period shall be reckoned from the date of the offer of such rights by the company or institution.
6. In case of a *bonus issue*, allotted without payment on the basis of holding of any other financial asset, period shall be reckoned from the date of allotment of such financial asset.
7. In case of shares in a resulting company received under a scheme of demerger of a company, the period for which the *shares in the demerged company* were held by the assessee will also be included.
8. In case of shares of trading or clearing rights of a recognised stock exchange acquired by a person under its demutualisation

or corporatisation, the period for which, such person was a member will also be included.

9. In case of equity shares allotted under demutualisation or corporatisation of a recognised stock exchange in India, the period for which such person was a member will also be included.
10. Period of holding of other capital assets will be decided according to the rules framed by the CBDT in that regard.

The CBDT has clarified that date of transfer/ acquisition of shares will be considered on the basis of the brokers' note / date of contract or date of allotment and FIFO (First in First Out Basis) in the case of Demat Accounts.

11. In case of security or sweat equity, shares allotted or transferred by the employer free of cost or at concessional rate to this employees including former employees, popularly called as ESOP, the period shall be reckoned from the *date of their allotment or transfer*.
12. The period of holding of units acquired in the consolidated scheme of mutual fund shall include the period for which the units in consolidating schemes were held by the assessee.
13. The period of holding of a capital asset, being share or shares of a company, acquired by a non-resident assessee on redemption of GDRs would be reckoned from the date on which a request for such redemption was made.

6. COMPUTATION OF CAPITAL GAINS- SEC. 48

8.1. General Rule

U/s 48 the income under the head "Capital Gains" shall be computed. by deducting from the full value of the consideration received or accruing as a result of the transfer of the capital asset the following amounts, namely :-

- (i) Expenditure incurred wholly and exclusively in connection with such transfer;
- (ii) The cost of acquisition of the asset and the cost of any improvement thereto:

8.2. Long Term Capital Gains

Where the capital gain is to be computed in respect of a long term asset, instead "cost of acquisition" and "cost of improvement", "indexed cost of acquisition" and "indexed cost of improvement" are to be deducted subject to following two exceptions, when benefit of indexation of cost will not be available, viz.-

- a.** On capital gain on transfer of shares or debentures of Indian company by a non-resident will be computed by converting the cost of acquisition, full value of consideration and expenses incurred for transfer into originally utilised foreign currency and reconverting capital gain into Indian currency.
- b.** On transfer of bonds and debentures even though they may qualify to be called long term capital assets. This is because bonds and debentures are normally issued and redeemed at par and if benefit of indexation is given, it will always give capital loss; and
- c.** In case of slump sale u/s 50B

Mode of computation can be depicted as under:

COMPUTATION OF CAPITAL GAINS			
Sales Consideration			
Less			
Expenses on Transfer			
Less			
Indexed cost of acquisition	Indexed Cost of Improvements	Cost of acquisition	Cost of Improvement
Long Term [LTCA]		Short Term [STCA]	

Note: The STCG / LTCG computed above are subject to deductions/exemptions under sections 54, 54B, 54D and 54EC, 54ED, 54F 54G etc.

8.3. Depreciable Capital Assets– Sec. 50

Where a capital asset has been sold or transferred and in respect of such capital asset depreciation had been allowed, the position will be as shown in the diagram below :

Depreciable Capital Assets			
Sales Consideration			
LESS	Expenses on Transfer		
LESS	Opening WDV	PLUS	New Purchase
▼			
IF WDV IS ZERO No Depreciation	Surplus Left Taxable as STCG	WDV still Remains	
		If Block Empty	Block Not Empty
		Short Term capital Loss No Depreciation	Claim depreciation

The detailed rules are as follows:-

- A. Written down value (WDV) of the block at the beginning of the year as increased by the cost of acquisition of any new asset falling in the same block purchased during the year and the incidental expense on transfer the asset purchased. The balance will be the written down value of the block and there will be no capital gain.
- B. If sales consideration exceeds the WDV of the block as increased by the new purchase and the incidental expense on transfer, such excess consideration will be treated as short term capital gain.
- C. If the resulting figure is negative, it will be treated as short term capital loss.
- D. If block ceases to exist, i.e., all assets in a block are sold, the WDV in the block will be short-term capital loss.

Thus, capital gain will arise only if the full value of sale price exceeds the aggregate of the following:-

- Incidental expenses on transfer
- The written down value of the block at the beginning of the previous year.
- Cost of acquisition of the asset falling in that block of assets during the previous year

The resulting figure will be short term capital gain or short term capital loss. If block cease to exist, no further deduction will be available and no further deduction will be allowed.

Illustration -4:

From the following particulars in respect of a block of assets :

- a. Opening WDV Rs 50,000
 - b. Cost of new asset purchased Rs 20,000
 - c. Rate of depreciation 20%
- Compute the depreciation or capital gain if _
1. No asset was sold during the year , or
 2. value of the consideration for asset sold was
 - b. Rs 70,000
 - c. Rs. 40,000
 - d. Rs. 1,00,000
 3. All assets in the block sold
 - e. Rs 40,000

Solution:

Particulars	a	b	c	d	d
	Rupees				
Opg WDV	50,000	50,000	50,000	50,000	50,000
Add-New Purchase	20,000	20,000	20,000	20,000	20,000
Total	70,000	70,000	70,000	70,000	70,000
Sales	0	70,000	40,000	1,00,000	40,000
WDV /Gain	70,000	0	30,000	(30,000)	30,000
Depreciation	14,000	0	6,000	0	0
STCG	-	-	-	30,000	-
STCL	-	NA	-	NA	30,000
Clos. WDV	56,000	0	24,000	0	0

Notes: No depreciation in case b as WDV in block comes to zero and in case e , all the assets are sold, hence the block ceases to exist. Residual WDV of Rs. 30,000 will be short term capital loss.

6.4. Depreciable assets of power undertaking: Sec 50A

In respect of a depreciable assets of an undertaking engaged in generation or distribution of power or energy, short-term gain/loss will be computed with reference to the cost of acquisition as adjusted u/s 43(6).

Land is not a depreciable asset. Hence, in case of a composite agreement for sale of a factory building along with the land, depreciable asset will be building. Land will be considered as general capital asset giving rise to long term or short term capital gain depending upon the period for which it is held.

6.5. Assets in Slump Sale – Sec. 50B

Slump sale means the transfer of one or more undertakings by way of sale for a lump sum consideration without assigning values to individual assets and liabilities of the undertaking.

In case of slump sale the undertaking itself will be treated as a capital asset and any profit on sale thereof shall be treated as long term or short depending upon the period of holding of such undertaking .

For the purposes of slump sale, 'net worth' [Sec. 50B (2)] of the undertakings shall be the cost of acquisition and improvement and no indexation u/s 48 is allowed in respect of such cost.

Net worth means the aggregate value of total assets i.e. WDV of depreciable assets and book value of other assets (excluding any revaluation of assets) as reduced by the value of liabilities of such undertaking or division

6.6. Sale of Land or building – Sec. 50C

U/s 50C in case of transfer of a capital asset being land or building or both, the sales consideration will be the higher amount of the following;

- the actual consideration received or accruing or
- value adopted or assessed or assessable by stamp duty authorities or the purpose of payment of stamp duty in respect of such transfer as on the date of transfer.
- Where the date of agreement and date of transfer are not same, stamp duty value on the date of agreement may be adopted as consideration, if whole or part of the consideration is paid by A/c payee cheque/bank draft or ECS through a bank A/c on or before the date of agreement.

If the assessee does not accept the stamp duty valuation and prefers appeal with the appellant authorities, the value finally determined shall be treated as the value of consideration.

However, if the assessee does not prefer any appeal but claims that agreement value is much lower than the valuation adopted by the stamp duty/registration authorities, the assessing officer may refer it for valuation. The consideration will not exceed the value adopted by the state authorities.

Illustration: 5

Agreement value of a land is Rs 5 Lakh. It is valued at Rs 4 lakhs only by the stamp duty authorities. Agreement Value Rs 5 lakhs will be taken as the consideration accruing for computing capital gains

Illustration: 6

Assuming the above land sold for Rs 5 lakh is valued at Rs 6 lakh by the stamp duty authorities, the consideration will be taken at Rs 6 lakh if the assessee does not dispute it.

Illustration: 7

If in the above case, the assessee, files an appeal with the stamp duty authorities, the consideration will be taken at the amount finally determined by those authorities.

Illustration: 8

If in the above case, the assessee, does not file an appeal with the stamp duty authorities, but disputes the stamp duty valuation, the assessing officer will refer the valuation to the Departmental Valuation Officer. However, such valuation cannot be more than Rs 6 lakhs.

6.7. Transfer of unquoted shares – Sec. 50CA

As per the newly introduced section 50CA from A.Y. 2018-19, where the consideration received or accruing as a result of the

transfer by an assessee of unquoted shares of a company, is less than the fair market value determined in the prescribed manner as per rule 11UAA, shall be deemed to be the full value of consideration received or accruing as a result of such transfer.

This section read with section 56 & 50C, will result into buyer and seller both having to pay the tax on difference of the FMV and the actual consideration.

Illustration

A transfers to B, unquoted shares costing Rs. 4 lakh for Rs. 8 lakh, while the FMV works out to Rs 10 lakh. As per section 50CA, FMV of Rs 10 lakh will be the amount of consideration. Capital gain of Rs. 7 lakh will be chargeable in the hands of A, while the inadequate consideration of Rs 7 lakh will attract section 56 (deemed gift) for B.

7. VALUE OF CONSIDERATION- SEC.48

“Full total value of consideration” means the value received or accruing because of the transfer.

It indicates the whole of the price; in terms of money or money's worth or both; bargained for between the parties *inter se*, which accrues or arises upon transfer of a capital asset.

The Capital gains will be chargeable on accrual basis and not on cash basis Actual receipt of the value is irrelevant.

Further, “full value of consideration” does not refer to the market value of the asset transferred or the adequacy of the price. However, there are some specific provisions, which require ascertainment of fair market value accruing or arising on transfer of a capital asset.

If the consideration cannot be expressed in money's worth, it will not form part of full value of the consideration for the transfer. Subject to the provision of Sec. 56, there will no capital gain in such a case. Some of such cases are as follows:-

- (i) In case of transfer of a property without consideration or out of natural love and affection or patriotism, subject to the provisions of Sec 56, there will no capital gain in such a case.
- (ii) in case transfer by a company as a gift or under an irrevocable trust of any shares, debentures, or warrants allotted directly or indirectly to its employees under employees' stock option scheme (ESOP/ESOS) as per the guidelines issued by the Central

Government, full value of the consideration will be the fair market value of shares on the date of transfer

(iii) In case of a transfer resulting in exchange of two or more assets, full value of consideration of the assets transferred will be equal to the fair market value of the asset received.

Illustration 9

A exchanges his flat for B's shop. In this case "Full total value of consideration of A's flat will be the fair market value of the shop transferred by B and vice versa.

(iv) Amount of any insurance claims received in respect assets destroyed in natural conditions like tsunami, floods, earthquakes, would be deemed the full value of consideration.

Sec. 45 specifies the year of the capital gain liability and the value of consideration arising or accruing in some cases, which are given in the following table :

Sub Section and the nature of the transaction	Previous year when taxed year of -	Value of consideration
(1) Sale or Transfer	Sale or transfer	Sales consideration
(1A) Damage or Destruction	Receipt of claim money	Money received or fair market value
(2) Conversion into stock	Sale of stock	Market value on the date of conversion
(2A) Transfer of securities by depository	Transfer determined on FIFO basis	Consideration for transfer
(3) Transfer as capital contribution in firm / AOP / BOI	Transfer	Value credited in capital account
(4) Transfer on dissolution of firm/AOP/BOI	Transfer	Fair market value on date of transfer
(5) Compulsory acquisition	Receipt of compensation	Initial compensation or enhanced compensation as the case may be
(6) Repurchase of mutual fund units	Receipt or discontinuation of scheme	Repurchase price

Illustration-10

A jeweller converted his personal bought gold ornaments for Rs 2,00,000 on 01/04/2001. On 01/01/2010, he converted the same into stock in trade of his business, when the fair market value of the ornaments was Rs. 7,00,000. On He sold the ornaments on 31/03/2018 for Rs. 12,00,000. Find out the tax incidence on this transaction .

Solution

Transfer takes place on 01/01/2010 being the date of conversion of personal gold into stock-in-trade and the amount of Capital gain will be:

	Rs
Full value of consideration [FMV 01/01/2010]	7,00,000
Less-Indexed Cost of Acquisition(revised) [2,00,000 X 148/100]	2,96,000
Long Term Capital Gain as on 01/01/2010	4,04,000

LTCG of Rs 4,04,0000 will arise on 01/01/2010 but be chargeable in A.Y. 2018-19, when actual sales of the ornaments took place .

In A.Y. 2018 -19, business profit of Rs 12 lakh- 7lakh= Rs 5 lakh will be taxable along with LTCG of Rs 4,04,0000 , which arose on 01/01/2010

10. COST OF TRANSFER – SEC. 48(1)

Expenditure incurred wholly and exclusively in connection with the transfer of asset will be deducted from the total value of consideration while computing the capital gain. This is subject to the following conditions:

- (i) The expenses should be incurred wholly and exclusively in connection with the transfer.

Lawyers' fee for transfer, brokerage, travelling expenses for transfer, advertisement, stamp duty and registration fee, if paid by the seller etc. will be allowable but normal administrative expenses like salary of staff for upkeep or maintenance of property will not be allowable .

- (ii) The expenses must not be claimed as deduction as expenditure under any other head.

- (iii) No expenses will be allowed in respect of share transactions covered under the securities transaction tax.

11. COST OF ACQUISITION – [SEC 48 - 46 & 49]

Cost of acquisition is the sum total of amounts spent for acquiring a capital asset including the following-

- (i) price paid by the assessee for purchase of property ; or
- (ii) fair value on the date of exchange , of the asset transferred in exchange, where the asset is acquired in exchange for another asset ; and

(iii) expenses incurred on transfer, registration, stamp duty etc.
The relevant provisions are given as under:-

Cost of Acquisition	
Date of Acquisition of Assets	
Prior to April,1,2001	April, 1,2001 on wards
Fair market value of asset as on 01/04/2001 –Optional	Actual cost paid for acquisition of asset

A. (1) Where the asset becomes the property of the assessee by a mode referred to in Sec. 49(1) before 1.4.81:

- i. Cost of acquisition is the actual cost to the previous owner or the fair market value as on **1.4.2001** at the option of the assessee.
- ii. Actual cost to the previous owner cannot be ascertained fair market value on the date on which the asset became the property of the assessee will be taken.
- iii. Where there are successive transfers under this mode, the reference to the previous owner will mean last of such previous owners who has acquired the assets by a mode otherwise than any of the modes u/s 49(1).
- iv. In these case the period for which asset was held by the previous owner is also taken into consideration to determine the period for which the asset was held

A. (2) Where the asset becomes the property of the assessee by a mode referred to in Sec. 49(1) on or after 1.4.2001:

- i. Cost of acquisition is the actual cost to the previous owner.
- ii. Actual cost to the previous owner cannot be ascertained fair market value on the date on which the asset became the property of the assessee will be taken.
- iii. Where there are successive transfers under this mode, the reference to the previous owner will mean last of such previous owners who has acquired the assets by a mode otherwise than any of the modes u/s 49(1).

B. (1) where the asset becomes the property of the assessee by a mode other than referred to in S 49(1) before 1.4.2001:

Cost of acquisition is the actual cost to the assessee or the fair market value as on **01-04-2001** at the option of the assessee. The base date has been advanced from 01/04/1981 to 01/04/2001 by the Finance Act, 2017

B. (2) Where the asset becomes the property of the assessee by a mode other than referred to in S 49(1) on 1.4. 2001 or thereafter:

Cost of acquisition is the amount actually spent by the assessee in acquiring the actual asset i.e. the actual cost of acquisition.

C. Where the asset becomes the property of the assessee subject to tax u/s 56 :

Where any asset (cash, movable property, or shares of closely held company's immovable property) is received without consideration or for consideration less than the fair market value, and as a result becomes taxable u/s 56, then, the cost of acquisition of such asset will be the cost taken u/s 56 for income tax purposes. The section is discussed in detail in the next chapter. The provision is apparently enacted to avoid double taxation of the same property.

D. Specific Cases:

i. Earnest money forfeited – S. 51;

Any earnest money received in advance and forfeited by the assessee, due to failure in negotiation is reduced from the actual cost of acquisition or the fair market value as on 01.04.2001 as the case may be and cost of acquisition will be adjusted accordingly. Now, earnest money forfeited will be taxable as "income from other sources". Hence, the provision of sec 51 will be applicable only if the earnest money was forfeited prior to that date.

Illustration-11

A acquired a building on May 12, 2010 for Rs. 28 lakhs. In 2014, He entered into negotiation with a prospective buyer, who gave him advance money of Rs. 5 lakhs at that time. However, the negotiations failed, and A forfeited the advance money. Subsequently, he actually sold the building in August 2017 for Rs 65 Lakhs. Calculate the indexed cost of acquisition and the taxable capital gains on the sale of the building.

Solution:

Particulars	Rs	Rs
Sales Consideration		65,00,000
Actual Cost	28,00,000	
Less: Earnest money forfeited-sec 51 (then not taxable)	5,00,000	
Net Actual Cost	<u>23,00,000</u>	
Indexed Cost of Acquisition $23,00,000 \times \frac{272}{167}$		37,46,108
Long Term Capital Gain		27,53,892

272 and 167 are the Index for financial years 2017-18 & 2010-11

As per new law w.e.f. 2017-18 earnest money would be taxable and in that case, cost of acquisition will not be adjusted

ii. Self-generated assets

The courts have taken the view that self-generating assets such as goodwill, patents, copyrights, tenancy rights, which have

no actual cost of acquisition incurred were not liable to capital gain tax as the cost of acquisition was Nil.

Now the amended law expressly provides that “ in relation to the *goodwill of a business, trade mark or brand name associated with a business, tenancy rights, loom hours, route permits, right to manufacture or produce any process any article, cost of acquisition shall be taken as the purchase price if such price is paid, or NIL, if such price is not paid.*”

Effectively, entire sale proceeds less expenses on transfer of self- generated assets will be treated as capital gain. An assets for a price from some other person, it will not be a self-generated assets and the other normal provisions of the Income Tax Act apply *mutatis mutandis**. (* with necessary modification)

iii. Financial assets – shares and other securities

Where an assessee becomes entitled to subscribe any additional securities, known as ‘Rights’ or where additional shares are issued as bonus i.e. without any payment, the cost of acquisition shall be as follows:

- a. Amount actually paid for acquiring such asset by way of *subscription to the securities*; or
- b. Amount actually paid for acquiring such asset by way of exercising his right or entitlement;
- c. NIL; where rights are renounced for a price, then consideration for renouncement of rights will be the amount of capital gains as reduced by transfer cost, if any;
- d. Amount paid to the renouncer of rights entitlement and amount paid to the company, which has allotted the rights shares;
- e. NIL in case of bonus shares- in other words, sales proceeds of bonus share will be liable to capital gain as reduced by transfer costs, if any. However, if the bonus shares have been acquired prior to 01-04-2001, then the share market value of bonus shares as on 01-04-2001 will be treated as the cost of acquisition;
- f. Fair Market Value on the date of distribution of capital assets by a Company u/s 46 (2);
- g. Cost of acquisition of the original asset Consolidation, division, conversion, reconversion of share into stock or vice versa and where such cost cannot be reasonably ascertained, the fair market value;
- h. Cost of acquisition of the original shares held by the shareholders in the demerged company as reduced by the amount arrived at u/s 49 (2C);

- i. Cost of acquisition of original membership of a recognised stock exchange when equity share/s allotted to shareholders of recognized stock exchange under a scheme of demutualisation or corporatisation of the exchange; – Sec. 55(2)(ab)
- j. NIL in respect of trading or clearing rights of stock exchange;
- k. *Pro rata* amount i.e. the amount which bears to the Cost of Acquisition of the shares held by the assessee in the demerged company the same proportion as the net book value of the assets transferred in a demerger bears to the net worth of the demerged company immediately before such demerger will be the cost of acquisition of Shares in the resulting company– Sec. 49 (2C);
- l. Stock option Specified security taxed as perquisites u/s 17(2) – Sec. 49 (2AA)
- m. Actual cost of acquisition in all the other cases.

12 FAIR MARKET VALUE

Fair market value, in relation to a capital asset, means the price that the capital asset would ordinarily fetch on sale in the open market on the relevant date. If the assessee has acquired the asset prior to 01-04-2001, he has the option of substituting the fair share market value of the asset as on 01-04-2001 instead of actual cost of acquisition. However, this option is available to the assessee only when the asset has been acquired prior to 01-04-2001. Fair market value is adopted in many cases like where ascertainment of actual cost is not possible; assets distributed on liquidation have already been dealt with at their appropriate places. Some other cases are considered below:

a) Conversion of capital asset into stock-in-trade

When the assessee converts a capital asset held by him into stock-in-trade of his business, it will be treated as taxable transfer giving rise to notional capital gains or loss. For this purpose, the fair market value of the capital asset on the date of conversion is treated as notional sale proceeds from which the cost of acquisition / indexed cost of acquisition is deducted in order to get the capital gain. Later, when this converted capital asset is sold there will be business profit or loss i.e. actual sale proceeds less notional fair market value taken, as cost will be the taxable business profit or loss. However business income as well as capital gains will be chargeable to tax only in the year of actual sale to a third party.

Illustration-12:

A jeweller converts his ancestral gold ornaments into the stock in-trade of his business on 1/1/2012. The ornaments are actually sold on 31/12/2017 for Rs. 22 Lakh. The market value of

the ornaments was Rs. 5 Lakhs on 01-04-2001 and Rs. 30 Lakhs on 1/1/2012.

Solution:

Capital gain arises on the date of conversion of a private asset into stock in trade

Cost of acquisition as on 01-04-2001 = Rs. 5 lakh.

Indexation in F.Y. 2011-12 – Index 184

LTCG = Rs 30 lakh – (Rs *5 lakh X 184/100)

= Rs 22 lakh - 09.20 lakh = Rs 12.80 lakh

Position 31/12/2017 (A.Y. 2018-19) - Date of Sales

Profit = Sales consideration – FMV on 01/01/2012

= Rs 22 lakh – Rs 5 lakh = Rs. 17 lakh

Amount taxable in A.Y. 2018-19

LTCG – Rs 12.80 lakh

Profits & gains of business & profession = Rs 17 lakh

b) Introduction of capital asset by a partner:

When a partner transfers his personal asset by way of his capital contribution in a partnership firm, the amount credited to his capital account in respect of this capital asset will be treated as sales proceeds in the hands of the partner from which the cost or indexed cost of acquisition will be reduced to get the amount of capital gains or loss taxable in the hands of the partner.

c) Takeover of assets by the partner on dissolution of the partnership firm

When a partner is allocated a capital asset upon the dissolution of a firm the fair market value of the capital asset on the date of dissolution of the firm will be treated as sales proceeds from which the cost of acquisition or indexed cost of acquisition, as the case may be, will be reduced to get the amount of taxable capital gains in the hands of the firm.

d) Compulsory acquisition of capital asset

Where there is compulsory acquisition of capital asset by the government or any government authority under law, there will be a taxable capital gain or loss in the year of such compulsory acquisition. However, such capital gain will be chargeable only in the year in which the compensation is received. If the compensation is enhanced later, then the receiver of such additional amount is chargeable to capital gains in the previous year in which such additional compensation is received. If the compensation amount is subsequently reduced, the capital gain already charged will be recalculated as if it were a mistake apparent from the record u/s 155.

d) Amount received by shareholder on liquidation of the company:

Out of the money received by the shareholder, a part of the amount will be treated as deemed dividend under section 2(22) and the remaining amount less the indexed cost of acquisition or cost of acquisition, as the case may be, is taxable as capital gains on sale of the shares.

f) Capital Gains on Sale of Shares under Depository System

Where an assessee has any depository account and any shares are sold from the depository account, then such cost of acquisition of the shares sold will be determined on FIFO i.e. on first in first out basis. It will be assumed that the assessee is shares deposited in the account first were sold first and accordingly the cost of acquisition, date of acquisition and the period of holding will be calculated.

g) Stock Lending

Any share given under the stock-lending scheme approved by SEBI in this behalf will not give rise to any taxable capital gain.

h) Corporatisation of Stock Exchanges

In case any person transfers equity shares allotted to him as member of a recognised stock exchange in India under a SEBI approved scheme of corporatization of stock exchanges, his original cost of acquisition of membership of the stock exchange will be the cost of acquisition for computation of capital gains on those shares.

i) Demerger:

Cost of acquisition of shares in the resulting company in case of a demerger shall be determined as follows:-

$$\frac{\text{Cost of shares of demerged company} \times \text{Net book value of assets}}{\text{Net worth of demerged company before demerger}}$$

The cost of acquisition of the original shares in the demerged company shall be reduced by the amount calculated as above.

j) Taxation of capital gains of listed shares

Share are treated separately by the provisions of sec. 111A/112, whereby an assessee is given the option to either pay a lump-sum tax of 18%+3% cess and forego the benefit of indexation or alternatively pay regular tax under the normal provisions including indexation .

13. TRANSACTIONS COVERED U/S 49(1):

U/s 49 in cases where capital asset became the property of the assessee in certain circumstances ,

- the cost of acquisition of the asset shall be deemed to be the cost for which the previous owner of the property acquired it,
- as increased by the cost of any improvement of the assets incurred or borne by the previous owner or the assessee, as the case may be.

These circumstances are as under :-

- (i) any distribution of assets on the total or partial partition of a Hindu undivided family;
- (ii) under a gift or will;
- (iii) by succession, inheritance or devolution,
- (iv) distribution of assets on the dissolution of a firm, body of individuals, or other association of persons, where such dissolution had taken place at any time before 01/04/1987,
- (v) distribution of assets on the liquidation of a company,
- (vi) under a transfer to a revocable or an irrevocable trust,
- (vii) under any such transfer as is referred to in clause (iv) or clause (v) or clause (vi) or clause (viaa) or clause (viab) or clause (vib) or clause (vica) or clause (vicb) or clause (vicc)] or clause (xiii) or clause (xiiib) or clause (xiv) of section 47;
- (viii) such assessee being a Hindu undivided family, by the mode referred to in sub-section (2) of section 64 at any time after the 31st day of December, 1969,
- (ix) under a gift or will not being gift or transfer through an irrevocable trust of shares, debentures or warrants allotted by a company directly or indirectly to its employees under a Central Government approved employees stock option (ESOP or scheme (ESOS). In such cases, the market value of the shares, debentures or warrants gifted or transferred to the irrevocable trust on the date of transfer will be treated as the sale proceeds for the purpose of capital gains;
- (x) by succession, inheritance or devolution;
- (xi) distribution of assets on liquidation of company;
- (xii) under a revocable or irrevocable trust;
- (xiii) on transfer by a wholly owned Indian subsidiary company from its holding company and by a parent company to its 100 per cent Indian subsidiary company;

- (xiv) on any transfer in scheme of amalgamation by the amalgamated company from the amalgamating company;
- (xv) by Hindu undivided family where one of the members has converted its self acquired property into a joint family property;
- (xvi) Transfer of units by unit holders on consolidation of plans within a mutual fund scheme;
- (xvii) Redemption by an individual of sovereign gold bonds issued by RBI;

Illustration-13

ABC HUF allotted a flat purchased by it on 01-04-2001 for Rs 5 Lakh to A as his share in HUF property on partition. A sells the flat for Rs. 30 lakhs on 1 April 2017. What will A's liability for tax?

Solution:

- a) There will be no liability for capital gain on 01-04-2001 as *partition of HUF is exempted u/s 49.*
- b) On 01-04-2017 relevant to A.Y. 2018-19, *cost and date of acquisition are same as previous Owner (HUF) viz Rs 5 lakhs and 01-04-2001.* The capital gain will be as under:

Sales consideration	30,00,000
Indexed cost of Acquisition $5,00,000 \times \frac{272}{100}$	<u>10,36,000</u>
LTCG	<u>29,64,000</u>

14. COST OF IMPROVEMENT:-S. 55(1)(B)

Cost of Improvement in relation to capital asset means any expenditure or cost of capital nature incurred by (a) *the assessee* or (b) the previous *owner* in case of an asset acquired by an assessee in any of the circumstances mentioned in S 49(1):-

- for substantially improving or raising the value of the capital asset or
- in making addition or alteration to capital asset after date of acquisition or
- for any expenditure incurred to protect or complete the title of the capital asset or
- to cure the title of the property or remove any defect from the title.

In other words, cost of improvement includes all those expenditures, which are incurred to increase the value of the capital asset

Following additional points are noteworthy in this regard

- (i) In case of a capital asset acquired prior to 01-04-2001, where the fair market value of the capital asset as of 01-04-2001 is substituted in place of cost of acquisition, all capital expenditure incurred by the assessee or the previous owner *after 01-04-2001* in making any additions or alterations to capital asset will be included in cost of improvement but **Cost of improvement incurred prior to 01-04-2001 will be ignored** in all cases.

The reason behind it is that for carrying any improvement in asset before 1st April 2001, asset should have been purchased before 1st April 2001. If asset is purchased before 1st April the fair market value is adopted and the fair market value of asset on 1st April 2001 will certainly include the improvement made in the asset.

- (ii) In any other case all the capital expenditure incurred in making in additions or alterations to the capital asset by the assessee after it become his property.
- (iii) There will be no cost of improvement to goodwill, right to manufacture or produce or process any articles or right to carry on any business.
- (iv) Expenditure deductible from the income from house property will not be included in cost of improvement.

15. INDEXED COST

Sec 48(iii), vide Expln iii defines Indexed Cost of Acquisition and Indexed cost of Improvement as under:-

"Indexed cost of acquisition" means:-

- an amount which bears to the cost of acquisition the same proportion as Cost Inflation Index for the year in which the asset is transferred bears to the Cost Inflation Index for the first year in which the asset was held by the assessee or for the year beginning on the 1st day of April, 2001, whichever is later; and

"Indexed cost of any improvement" means:-

- an amount which bears to the cost of improvement the same proportion as Cost Inflation Index for the year in which the asset is transferred bears to the Cost Inflation Index for the year in which the improvement to the asset took place; and

"Cost Inflation Index" (CII) for any year means:-

- Such Index as the Central Government may, having regard to seventy-five per cent of average rise in the Consumer Price Index for urban non-manual employees for that year, by notification in the Official Gazette, specify in this behalf

Indexed cost of acquisition/ improvement can be shown by the following formulae:

Indexed cost of acquisition

Cost of Acquisition X CII (the year of Transfer)
CII in the year of acquisition or 01-04-2001 , whichever is later

Indexed Cost of Improvement

Cost of Improvement X CII (the year of Transfer)
CII in the year of Improvement

Exceptions:

Indexation benefit is not available in respect of the following:

1. Short term capital assets
2. Bonds / debentures other than Capital Indexed Bonds Issued by Government;
3. Shares/Debentures of Indian Company Purchased in Convertible Forex by non-residents
4. Depreciable assets
5. Units Purchased in Foreign Currency u/s 115AB by Offshore Fund
6. GDRs purchased in Foreign Currency u/s 115AC Non-Residents
7. Securities u/s 115AD purchased by non-residents
8. Where option of 15% tax rate is claimed/s 112 in respect of capital gain on shares
9. Slump Sale u/s 50B
10. Foreign exchange assets u/s 115-O by Non- Resident Indians.

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

16. TRANSACTIONS NOT ‘TRANSFER” –SEC 46, 47

A. Section 47 provides that following transactions will not be regarded as transfer for the purpose of section 45 :

- 1) any distribution of capital assets on the total or partial partition of a HUF ;
- 2) any transfer of a capital asset under a gift or will or an irrevocable trust not being issue of securities allotted under ESOP or ESOS by a company to its employees ;
- 3) any transfer of a capital asset not being an asset transferred as stock in trade by a:-
 - (a) by a holding company to its 100% Indian subsidiary company or
 - (b) 100% subsidiary company to its Indian holding company,

- 4) any transfer, in a scheme of amalgamation,
 - (a) of any capital asset by the amalgamating company to an Indian amalgamated company or ;
 - (b) of any shares held in an Indian company by the amalgamating foreign company to the amalgamated foreign company if at least 25% of the shareholders of the amalgamating foreign company continue to remain shareholders of the amalgamated foreign company, and such transfer does not attract tax on capital gains in the country, in which the amalgamating company is incorporated;
 - (c) of any capital asset by a banking company to a banking institution if such scheme is u/s 45(7) of the Banking Regulation Act, 1949;
 - (d) of any shares held by a shareholder in the amalgamating company, made in consideration of the allotment to him of any share or shares in an Indian amalgamated company ;
- 5) any transfer, in a scheme of demerger,
 - (a) of a capital asset by the demerged company to the resulting Indian company;
 - (b) of shares held in an Indian company, by the demerged foreign company to the resulting foreign company, if the shareholders holding not less than $\frac{3}{4}$ th in value of the shares of the demerged foreign company continue to remain shareholders of the resulting foreign company and such transfer does not attract tax on capital gains in the country, in which the demerged foreign company is incorporated
 - (c) any transfer or issue of shares by the resulting company, to the shareholders of the demerged company if the transfer or issue is made in consideration of demerger of the undertaking;
- 6) any transfer in a business reorganisation,
 - (a) of a capital asset by the predecessor co-operative bank to the successor co-operative bank;
 - (b) of shares in the predecessor co-operative bank by a shareholder, made in consideration of the allotment to him of any share or shares in the successor co-operative bank.

- 7) any transfer of bonds or Global Depository Receipts U/s 115AC (1), made outside India by a non-resident to another non-resident;
- 8) any transfer of agricultural land in India effected before 01/03/1970 ;
- 9) any transfer of any work of art, archaeological, scientific or art collection, book, manuscript, drawing, painting, photograph or print, to the Government or a notified University or the National Museum, National Art Gallery, National Archives or any such other public museum or institution ;
- 10) any transfer by way of conversion of bonds or debentures, debenture-stock or deposit certificates in any form, of a company into shares or debentures of that company;
- 11) any transfer by way of conversion of bonds referred to section 115AC (1)(a) into shares or debentures of any company;
- 12) any transfer membership of a recognised stock exchange to a company made on or before 31/12/1998 by a person (not being a company) in exchange of shares allotted by that company to the transferor;
- 13) any transfer of land of a sick industrial company managed by its workers' co-operative during the period of loss till the period upto which the company's losses are equal to or more than its capital), under rehabilitation scheme U/s 18 of the Sick Industrial Companies (Special Provisions) Act, 1985;
- 14) any transfer of a capital asset or intangible asset by a firm to a company as a result of succession of the firm by a company in the business carried on by the firm, or any transfer of a capital asset to a company in the course of demutualisation or corporatisation of a recognised stock exchange in India as a result of which an association of persons or body of individuals is succeeded by such company if:
 - (a) all the assets and liabilities of the firm or of the association of persons or body of individuals relating to the business immediately before the succession become the assets and liabilities of the company;
 - (b) all the partners of the firm immediately before the succession become the shareholders of the company in the same proportion in which their capital accounts stood in the books of the firm on the date of the succession;

- (c) the partners of the firm do not receive any consideration or benefit, directly or indirectly, in any form or manner, other than by way of allotment of shares in the company; and
 - (d) the aggregate of the shareholding in the company of the partners of the firm is not less than fifty per cent of the total voting power in the company and their shareholding continues to be as such for a period of five years from the date of the succession;
 - (e) the demutualisation or corporatisation of recognised stock exchange in India is carried out under an approved scheme
- 15) any transfer of a membership right held by a member of a recognised stock exchange in India for acquisition of shares and trading or clearing rights acquired by such member in that recognised stock exchange under an approved scheme for demutualisation or corporatisation ;
- 16) any transfer of a capital asset or intangible asset by a private company or unlisted public company to a limited liability partnership or any transfer of a share or shares held in the company by a shareholder as a result of conversion of the company into a limited liability partnership if –
- (a) all the assets and liabilities of the company immediately before the conversion become the assets and liabilities of the limited liability partnership;
 - (b) all the shareholders of the company immediately before the conversion become the partners of the limited liability partnership and their capital contribution and profit sharing ratio in the limited liability partnership are in the same proportion as their shareholding in the company on the date of conversion;
 - (c) the shareholders of the company do not receive any consideration or benefit, directly or indirectly, in any form or manner, other than by way of share in profit and capital contribution in the limited liability partnership;
 - (d) the aggregate of the profit sharing ratio of the shareholders of the company in the limited liability partnership shall not be less than fifty per cent at any time during the period of five years from the date of conversion;
 - (e) the total sales, turnover or gross receipts in the business of the company in any of the three previous years preceding the previous year in which the conversion takes place does not exceed sixty Lakh rupees; and

- (f) no amount is paid, either directly or indirectly, to any partner out of balance of accumulated profit standing in the accounts of the company on the date of conversion for a period of three years from the date of conversion.
- 17) Any transfer of any capital asset or an intangible asset upon conversion of proprietary concern into a company, if
 - (a) all the assets and liabilities of proprietary concern become the assets and liabilities of the company upon such conversion ;
 - (b) sole proprietor holds 50% or more of the total voting power for a period of five years from the date of the succession; and
 - (c) the consideration is paid by way of allotment of shares in the company and not in any other form;
- 18) any transfer in a scheme for lending of any securities under an agreement or arrangement, between the lender and the borrower .
- 19) any transfer of a capital asset in a transaction of reverse mortgage under a scheme made and notified by the Central Government.
- B. Similarly, U/s46(1) ,any distribution of assets of a company under liquidation by the liquidator to the shareholder is not regarded as transfer because such distribution is deemed as dividend u/s 2(22);

17. LLUSTRATIONS

Illustration 11

State whether the following are the capital Asset or not:

1. Bicycle
2. Horse
3. Car
4. House for self residence
5. Jewellery
6. House let on hire
7. Silver utensils
8. Air Conditioner used as stock in trade
9. Air Conditioner not used as stock in trade
10. Rural Agricultural Land
11. Urban Agricultural Land

Solution:

Items 1,2,3,7 & 9 **Bicycle , horse , personal air conditioner and silver utensils** (if used for personal use) are personal effects, hence not capital assets .

Item 8 **Air Conditioner** used as stock in trade and Item 10 **Rural agricultural land** are excluded from the definition of capital asset.

All the remaining items are capital assets including , Item 4 House for self residence, item 5 Jewellery , item 6 House let out on hire, item 7 Silver utensils and item 11 Urban agricultural land as they are not excluded from the definition of capital asset .

Illustration-12

State whether the following transactions are transfer :

1. A house transferred by way of will to son.
2. Bonus shares given by a company to its shareholders.
3. Giving away jewellery for a piece of land.
4. Getting money in lieu of shop in a shopping complex.
5. Giving the rights to use the asset.

Solution

- 1) Transfer by will is not transfer.
- 2) Issue of Bonus share is not transfer.
- 3) Exchange of jewellery with land is transfer of both assets.
- 4) Money being consideration of shop, It is transfer.
- 5) Not transfer as asset only hired.

Illustration -13:

An asset was acquired on 31 May 2001 for Rs 10,000, it is substantially improved on 30 June 2004 for Rs 5,000 and it is sold on 10 December 2015 for Rs 75,000.

Solution:

Particulars		Rs
Sales consideration		75,000
Indexed cost of acquisition (10,000* 272/100)	27,200	
Indexed cost of improvement 5,000 X 272/113).	<u>12,035</u>	<u>39,235</u>
Long Term Capital Gain		<u>36,765</u>

Illustration-14

Assume that the asset was acquired before 01-04-2001 & and improvement were carried before 01-04-2001 there is no change in fair market value on 01-04-2001.

Sales consideration		75,000
Indexed cost of acquisition (10,000 X 272/100) on 01-04-2001*	27,200	
Cost of improvement Ignored (Pre-01/04/1981 *Optional)	<u>0</u>	<u>27,200</u>
Long Term Capital Loss		47,800

Illustration-15

A sells a residential house property in Mumbai for Rs. 30,00,000 on May 15, 2017. The house was purchased by him on June 11, 2002 for Rs 2,00,000. Compute the capital gain-

Solution:

Sales Consideration.	Rs. 30,00,000
Less- Indexed cost of acquisition 9,00,000 X 272/105	23,31,413
Long Term Capital Gain	<u>6,68,587</u>

Illustration-16

A sells a flat on 13 March 2018 for Rs 7,00,000. He had acquired the flat on 15 August 1993 for Rs 1,00,000 and had incurred capital cost of major repairs of Rs 50,000 in 1994-95.

Solution

Sales Consideration		Rs. 7,00,000
Indexed cost of acquisition (1,00,000*272/113)	2,40,708	
Indexed cost of improvement (50,000* 272/129)	1,05,426	3,46,134
Long Term Capital Gain		3,53,286

Illustration-17:

X purchased a house property for Rs. 4,00,000 01/07/2015 and constructed the first floor in March 2016 for 1,10,000. The house property was sold for Rs 7,10,000 31/03/2018. The expenses incurred on transfer of asset were Rs. 10,000. Compute the capital gains from the transaction and show the difference, if any, if the house was constructed in March, 2016

Solution:

Sales consideration		7,10,000
Less: Expenses For Transfer		10,000
Net Sales Consideration		7,00,000
Indexed cost of acquisition 1 lakh * 272/254	4,28,465	
Indexed cost of improvement 1,10,000 x 272/254	1,17,795	5,46,260
Long Term Capital Gain		1,53,746

Notes: 1. Date of purchase will be the date of acquisition. Construction of additional floor is improvement to the property.

2. If the house was constructed in March, 2016, it is held for 24 months, which is less than 36 months. It will be short term capital asset not entitled to indexation. Resultant capital gain of Rs 2,90,000 will be Short Term Capital gain [Rs. 700000- (4,00,000+ 1,10,000)- 4,90,000]

Illustration 18.

On 01/07/2017 X sold gold jewellery for Rs.1,10,000. It was purchased on 01/07/1970 for Rs 9000. Market Value of the jewellery as on 1st April 2001 was Rs. 40,000 compute taxable amount of capital gain, if the expense on transfer is 5% on sales price.

Solution:

Sales Consideration		Rs. 1,10,000
Less: Indexed Cost of Acquisition cost as on 01/04/2001 -40,000 x 272/100	1,08,100	
Expenditure on transfer (0.5% x 1,10,000)	550	1,08,350
Long Term Capital Gains		1,650

Illustration-19:

X invested Rs. 1,00,000 in ornaments and Rs. 50,000 in equity shares on 1st March 2015. He sold the jewellery for Rs. 1,20,000 and shares for Rs.1,00,000 on 1st August 2017. There was a ½% brokerage on both the investments, both at the time of purchase and sale. Calculate the taxable amount of capital gain.

Solution:**A- Capital Gain on sale of Jewellery**

Particulars	Rs.	Rs.
Sales Consideration of Jewellery		1,20,000
Less: Cost of Acquisition	1,00,000	
Brokerages on purchases (0.5% x100,000)	500	
Brokerages on Sales (0.5% x120,000)	600	1,01,100
Short Term Capital Gain		<u>18,900</u>
Jewellery held for 30 months (1/3/2015 to 1/8/2017) less than 36 months, hence STCG, no indexation.		

B- Capital Gain on sale of Shares

Particulars	Rs.	Rs.
Sales Consideration on Sale of Shares		1,00,000
Less: Indexed Cost of Acquisition	50,000	
Brokerages on purchases (0.5% x 50,000)	250	
50,250 * 272/240	56,950	
	81,073	
Brokerages on Sales (0.5% x 1,00,000)	500	56,450
Long Term Capital Gain		43,550

18. SELF ASSESSMENT QUESTIONS:

- Write short note on:
 - Short Term Capital Gain
 - Cost of Acquisition
 - Cost of improvement
 - Expenditure on transfer
 - Transfer
- Explain the term 'capital asset'.
- Explain capital gains on compulsory acquisition of a capital asset.
- What is "transfer" in relation to a capital asset?
- State the situations under which the written down value of a "block of assets" will be reduced to nil.
- Give any five items are not considered as 'capital asset'.
- Explain the provisions of the Income Tax Act, 1961 regarding:
 - Conversion of capital assets to stock-in-trade.
 - Computation of capital gains in case of depreciable assets.
- State whether the following are the capital Asset or not:
 - Bicycle
 - Horse
 - Car
 - House for self residence
 - Jewellery
 - House let on hire
 - Silver utensils
 - Air Conditioner used as stock in trade
 - Air Conditioner not used in own house
 - Rural Agricultural Land
 - Urban Agricultural Land

{Ans: item g is not capital asset}

9. Whether the following transactions are transfer in relation to capital asset.

- a. A house transferred by way of will to son.
- b. Bonus shares given by a company to its shareholders.
- c. Giving away jewellery for a piece of land.
- d. Getting money in lieu of shop in a shopping complex.
- e. Giving the rights to use the asset.

[Ans: only c and d are transfers]

10. M sold his house in Mumbai on 15/04/2015 for Rs 6.5 Lakh. He had purchased it at a cost of Rs. 50,000 on 03 / 07 / 1983. The purchaser paid Rs. 4 lakhs 01/05/2015 and the balance on 30/06/2015 M paid brokerage of Rs. 13,000 for the sale transaction. Compute the total taxable capital gain. (Ans: LTCG 1,71,052 i.e. $6,50,000 - 13,000 - 4,65,948 = \{50,000 \times 1081/116\}$)

11. S purchased shares in unlisted Indian companies on 10/06/2011 for Rs. 2,00,000. On 1/06/2000 he started a business as a dealer in shares and transferred the entire holdings to the business. The market value of the shares as on that date was Rs. 8,00,000. He sold the shares Rs. 9,20,000 on 30/10/2017. Compute taxable capital gains.

(Ans: LTCG Rs. 8,00,000 - Rs. 2,00,000 $\times 254/182 =$ Rs. 5,20,879 for AY 2001-2002 & Business Profits Rs. 1,20,000 taxable in AY 2018-19)

12. Aditya sold his only house property occupied by him as residential house for Rs 18 lakh on 31/12/2017. The house property was purchased by him on 28/02/2005 for a consideration of Rs 2 lakhs. Determine the capital gains.

(Ans: LTCG Rs 3,18,484 = $[18,00,000 - 17,29,600] (Rs. 2,00,000 \times 272/113)$

13. Siddharth converts his plot of land purchased in July 2006 for Rs 60,000 into stock-in-trade on 31st March 2014. The fair market value on 31.3.2014 is Rs 1,60,000. The stock-in-trade was sold for Rs 2,00,000 in the month of January 2018. Find out the taxable income, if any, and if so under which "head" of income and for which "assessment year".

(Ans: LTCG $1,60,000 - 60,000 \times 220/112 =$ Rs. 91,803 in AY 2014-2015. & Business Income Rs. 40,000 taxable in AY 2018-19)

14. X acquired a plot of land on 30.6.2006 for Rs. 2,20,000. Brokerage and other incidental expenses on acquisition of plot were Rs. 30,000. X sold the plot of land on 30.6.2017 for Rs. 12,50,000. What will be the amount of capital gain? Can he claim deduction for ground rent paid by him amounting to Rs. 5,000 during the period when he held the asset?

(Ans: LTCG $12,50,000 - 2,50,000 \times 272/122 =$ Rs. 7,43,622, No)

15. Y Purchases 250 equity shares of ABC Ltd on 01/04/2011 @ Rs. 270 per share and incurs Rs. 500 on brokerage and transfer. On 01/07/2012, he gets 200 bonus shares. On 01/09/2014 he gets 300 right shares @ Rs 140 per share. On 28/02/ 2018 he sells all the 750 shares@ Rs 1000 per share and incurs expenditure of Rs. 1,500 on brokerage. Compute his taxable capital gain.

(Ans: Sales $[750 \times 1000] - 1500 - \text{Purchase } [250 \times 270 + 500] \times 272/184 + 0$
 Bonus + Right $[300 \times 140] \times 272/240 = 47,600$ LTCLG Rs. 5,99,278) {7,48,500 =
 $[1,00,522 + 0 + 47,600]$



INCOME FROM OTHER SOURCES

(Sections 56 -59)

Synopsis:

1. Introduction & Objectives
2. Basis of Charge
3. Incomes specifically chargeable u/s 56
4. Other incomes chargeable u/s 56
5. Some specific incomes – gifts, dividend
6. Deductions
7. Amounts not deductible
8. Miscellaneous- Balancing charge, Method of accounting
9. Self- Assessment Questions

1. INTRODUCTION AND OBJECTIVES

Of all the heads of income specified in section 13, “income from other sources is the last and residuary head of income. Income not covered under any other head of income, will be chargeable to tax under this head. The lesson explains the scope of “Income from other sources”, its computation and the deductions allowable therefrom as given in section 56 to 59.

2. BASIS OF CHARGE- SECTION 56

2.1. As per section 56 (1), any income, which is not chargeable to tax under any other heads of income and which is not to be excluded from the total income shall be chargeable to tax as residuary income under the head “Income from Other Sources”.

2.2. As per section 56(2), the following incomes are specifically chargeable to tax under the head “Income from Other Sources”:-

- i. Dividends
- ii. Any winnings from lotteries, crossword puzzles, races including horse races, card games and other games of any sort or from gambling or betting of any form or nature whatsoever.

- iii. Any sum received by the assessee from his employee as contribution towards provident fund , superannuation fund or Employee State Insurance fund or any other employees' welfare fund, if not chargeable under the head 'profits and gains of business or profession'.
- iv. Interest on securities, if not chargeable under the head 'profits and gains of business or profession'.
- v. Rental income from machinery, plant or furniture belonging to the assessee and let on hire if not chargeable under the head 'profits and gains of business or profession.'
- vi. Composite rental income from letting machinery, plant or furniture with buildings and letting of the buildings is inseparable from the letting of the said machinery, plant or furniture, if not chargeable under the head 'profits and gains of business or profession'.
- vii. Any sum including bonus received under keyman insurance policy, if not taxable as salary or 'profits and gains of business or profession'.
- viii. Any sums of money exceeding Rs. 50,000 in aggregate received without consideration by an individual or HUF.
- ix. Fair market value of movable property received without consideration by an individual or HUF if it exceeds Rs 50,000 in aggregate.
- x. The difference between the aggregate fair market value and the consideration received by an individual or HUF in respect of a movable property or immovable property, if such difference exceeds Rs 50,000.
- xi. The stamp duty value of any immovable property (whether assessed or assessable) if it exceeds by Rs 50,000 than the consideration for such immovable property received by an individual or HUF.
- xii. Shares of closely held companies having aggregate fair market value exceeding Rs. 50,000 received by a firm or a closely held company without consideration or for a consideration which is less than the aggregate fair market value of the property by an amount exceeding Rs 50,000.
- xiii. Interest received on compensation or on enhanced compensation referred to in section 145A (b).
- xiv. Any sum of money received as an advance or otherwise in the course of negotiations for transfer of a capital asset, if such sum is forfeited and the negotiations do not result in transfer of such capital asset.

3. INCOMES SPECIFICALLY CHARGEABLE -S. 56(2)

In addition to the residuary income chargeable to tax but not covered under other heads of income, the head “income from other sources” also covers some well-defined income given as under:-

- i. Dividend received from any entity other than a domestic company; The dividend received from a domestic company is exempt under section 10(34), because dividend is taxable in the hands of the company at the time of distribution and 18% dividend distribution tax is levied u/s 115(0). Dividend received from a cooperative bank or a foreign company, and dividend received by individual and HUF assesseees in excess of Rs 10 lakh (gross without any deduction for expenses) will be chargeable under this head.
- ii. Pension received by the legal heirs of an employee; Pension received by the employee himself during his lifetime is charged under section 17(3) as the income from salaries;
- iii. Any winnings from lotteries, crosswords, puzzles, races including horse races, card games or other games of any sort or gambling or betting of any form or nature;
- iv. Income from letting out any plant, machinery or furniture on hire where it is not the business of the assessee to do so;
- v. Interest on securities if it is not chargeable as the profit and gains of business or profession.
- vi. Employees' contribution to any staff welfare scheme received by the employer, which is not paid within the prescribed time. However, deduction will be allowed in respect of the amount of contribution paid, only the balance amount will be taxable;
- vii. Income from sub-letting;
- viii. Interest on bank deposits and loans and securities;
- ix. Royalty;
- x. Directors' fees;
- xi. Casual income;
- xii. Agricultural income when taxable e.g. land situated in a foreign country,
- xiii. Income from undisclosed sources;
- xiv. Rent of plot of land;
- xv. Mining rent and royalty;
- xvi. Casual income under a will, contract, trust deed;
- xvii. Salary payable to a member of parliament;

- xviii. Gratuity received by a director who is not an employee of a company; and
- xix. Any other receipt, which is income but does not fall under the other four heads of income viz. salary or business income or income from house property or capital gain.

4. SOME SPECIFIC INCOMES :

5.1. Dividend - Sec 56(2) (i)

Dividend is the amount of profits distributed by a company among its shareholders or members. Some important principles concerning the dividend are given as under: -

1. Taxable amount of dividend shall be chargeable as income from other sources.
2. It is not relevant whether dividend is :-
 - in cash or kind or
 - out of taxable profits or tax -free income,
 - out of revenue profits or capital gains.
3. Dividend is of three types :
 - a) Final dividend ;
 - b) Interim Final dividend; and
 - c) Deemed dividend
4. Final dividend is declared at the at the annual general meeting of a company (AGM), where the final accounts for the financial year are laid before the members. Final dividend is chargeable to tax on the date of AGM, when it is declared. Date of actual payment of the dividend is not relevant. Final dividend, once declared becomes a debt due and cannot be withdrawn as in case of non-payment it is earmarked in a separate account as per the Companies Act, 2013.
5. The dividend declared by the board of directors between two AGMs is called Interim dividend. Interim dividend will be taxable when it is made available or paid to the shareholder.
6. Deemed dividend is not dividend in real terms. Certain payments made to shareholders by the company or its liquidator are deemed to be dividend in the hands of the shareholder in different circumstances prescribed in Section 2(22) and are chargeable under the head income from other sources when such sums are actually paid .

7. Dividend received from a domestic company shall be exempt from tax under Section 10(34) if it is chargeable to dividend distribution tax under Section 115-O.

8. As per section 115BBDA, in the case of resident individual/HUF/firm, dividend shall be chargeable to tax at the rate of 10% if aggregate amount of gross dividend received during the year exceeds Rs. 10,00,000

5.2. Deemed dividend: - Loan to shareholders- S. 2(22) (e)

Under Section 2(22) (e) any sum paid as loan or advance by a closely held company

- to a shareholder for his individual benefit, and if such shareholders and his relatives holds substantial interest (10 per cent stake in share capital or voting power)in the company or
- to a concern(HUF/Firm etc) where the person having substantial interest has at least 20 per cent interest, shall be deemed to be the dividend in the hands of the shareholder.

This provision intend to prevent persons having substantial control and influence over the affairs of a company to take away all funds of the company as low-interest loans for their personal benefit to the prejudice of the other shareholders.

Some other important points are relevant: -

1. Dividend income will be taxable in the hands of the recipient in the year in which such loan or advance was given- Sec 8.
2. The section will apply only on cash loans or advances.
3. Advances made in kind e.g. of sale of goods on credit in the normal course of business will not be deemed to dividend.
4. Dividend will be chargeable even if the loan or advance has been repaid. The courts have repeatedly held that there is no inequity in this;
5. A shareholder is entitled to set off the deemed dividend if and when company declares any dividend. In practice, since the dividend is tax-free in the hands of the shareholder, the set –off provision does not grant any real benefit of set-off to the shareholder;
6. The loan will be taxable as dividend only to the extent of free reserves of the company;
7. Loans or advance made by the lending company for which lending is the main or substantial part of its business will also not be covered by this section;
8. Any advance or loan made to a shareholder or the concern by a company in the ordinary course of its business, for purchase

of its own shares or on demerger etc will also be not be covered under this section;

9. The deemed dividend will also be subject to dividend distribution tax @30%.
10. Substantial interest may be existing at any time during the year;
11. Any deemed dividends u/s 2(22) (e) or dividend from any other entity is, however taxable in the hands of the recipient; and.
12. Deduction of expenses on collection and interest on loan, taken for investment in shares, is available against dividend income.

Illustrations

Ascertain the amount of deemed dividend u/s 2(22) (e) in the following situations. The companies are closely held, and the shareholder has substantial interest therein.

1. A borrows Rs 20 as loan from A Ltd. and returns the loan next day, when he makes his own arrangement for finance. The Company was had free reserves of Rs 10 lakh.

Solution

Out of the loan amount of Rs 20 lakh , only Rs. 10 lakhs , to the extent of free reserve of A Ltd. will be treated as deemed dividend u/s 2(22)(e). Repayment of loan does not affect the tax liability. A is entitled to setoff dividend against dividend If and when declared.

2. A takes a loan of Rs 20 lakhs from B Ltd., having free reserves of Rs 20 lakhs.

Solution:

Entire loan amount of Rs 20 lakhs will be deemed dividend in the hands of B U/s 2(22) (e)

3. In the above case, assume B Ltd is a loss making company having no free reserves

Solution

Since B Ltd. has no free reserves, the loan taken will not be taxable in the hands of A as dividend.

4. A takes a temporary loan of Rs 20 lakhs from D Ltd., for one month only. Thereafter, he transfers the shares. The Company was having free reserves of Rs 20 lakhs.

Solution :

Entire loan amount of Rs 20 lakhs will be deemed dividend in the hands of B u/s 2(22) (e), even if A holds substantial interest only for a part of the year.

5.3. Deemed dividend – Distribution by Companies: S. 2(22)

Any distribution by a company to its shareholders which entails the assets of the company, or distribution made on liquidation or reduction of capital is regarded as dividend to the extent of accumulated profits of the company.

Similarly, any distribution by a company to its preference shareholder or debentureholders is also regarded as deemed dividend to the extent of accumulated profits of the company. Dividend in this class is directly taxable in the hands of the company.

5.4. Interest on securities

Interest received from debentures of company, mutual funds, and government securities is taxable as income from other sources except when such income is exempt u/s 10 or is taxed as business income. If any tax is deducted at source from interest on such securities, it should be added back and only the gross income should be considered. However, in case of tax-free govt. securities, grossing up is not required as there is no deduction or TDS. However, grossing up is required in case of taxable securities and non-government securities.

From the Interest income from this head, reasonable bank charges and other collection charges, office and other expenses if the same were incurred for earning the income and interest payable on loans taken for acquiring securities can be deducted.

Illustration -5

A received Rs 36,900 as interest net of TDS @ 10% on debentures of B Tea Ltd worth Rs 2,50,000 held by him. Calculate the interest income and the amount of TDS @ 10% that can be claimed.

Solution:

Dividend received net of 10% TDs:	Rs 36,900
Gross Dividend – $36000/90\%$:	Rs 41,000
TDS claim 10 % of Gross dividend	Rs 4,100

5.5. Winning from Lotteries, Crossword puzzles, etc

Winnings from, Lottery, crossword puzzles, card games or other games including any game show like KBC and horse races, betting, gambling etc are all treated as income from other sources and taxed at the maximum marginal rate u/s 115BB on the gross income without considering :-

- Claiming basic exemption limit
- Deductions under chapter VI-A.
- Expenditure including collection charges, etc or allowances;
- Benefit of set off and carry forward of losses.

Illustration 6

The winnings out of Sawaal Aapka were Rs 1,50,000. Calculate the net receipt.

Solution :

Winning received subject to maximum marginal rate is 30%, + 3% education cess and the secondary and higher education cess (total 30.9%) payable at source.

Hence, gross winning – (Rs 1, 50,000 X 30.9%)	Rs 46,350
Net receipts of winnings - (Rs 1, 50,000 – Rs 46,350)	Rs 1,03,650
Alternatively – Rs 1,50,000 X 69.1%	= Rs 1,03,650

5.6. Family Pension

Family pension means a regular monthly payment made to the legal heirs of the employee after his death. This is treated as income from other source and not salary because there is no employer-employee relationship between the legal heirs and the employer.

Standard deduction equal to 1/3rd of the pension or Rs. 15,000 is available as deduction from this income. Significantly, pension amount received during the lifetime of employee is taxable as salaries u/s 17(3) and not entitled to standard deduction.

Illustration 7

Mrs. S receives Rs 75,000 as yearly pension after the death of her husband. She pays Rs 2,000 per month to Ali to collect it from the office of the employer. Calculate the net taxable pension of Mrs. S.

Solution

Pension amount	Rs 75,000
Less: Lower of the following :	Rs 15,000
• 1/3 rd of the pension i.e. =	
Rs 75,000 X 1/3 = Rs 25,000 or	
• Rs 15,000	
Taxable Pension	Rs 60,000

The expenses occurred for collection of family pension to the extent of Rs 24,000 shall not be allowable as deduction since the standard deduction of 1/3rd of family pension or Rs 15,000 is to cover such expenses.

4.7. Gifts in the hands of individuals and HUFs:

In a major deviation to the principle that income tax is a tax on income, not on capital receipts; the Finance Act, 2004 amended section 56 to bring gifts under the tax net. Since then, the section

has been amended several times to widen the scope of taxable gifts. The latest legal position is summarised as follows:

5.7.1 Taxable Gifts

U/s 56(2) ((vii), Following receipts by an individual or a Hindu undivided family, in any previous year from any person or persons will be taxable as "Income from Other Sources":

- a. Any sum of **money, without consideration, the aggregate value** of which Rs 50,000 , the whole of the aggregate value of such sum
- b. Any **immovable property**,
 - i. **without consideration**, the stamp duty value of which Rs 50,000, the stamp duty value of such property;
 - ii. for a **consideration** which is less than the stamp duty value of the property by an amount exceeding Rs 50,000,

Following points are important in this regard :

5.7.2 Date of valuation

When the date of agreement and the date of registration are not the same stamp duty value will be considered on :-

- the date of agreement if any part or whole of the amount of consideration thereof, has been paid by any mode other than cash on or before the date of the agreement;
- the date of registration in all other cases .

5.7.3 Disputed Value

If the stamp duty value of immovable property is disputed by the assessee u/s 50C (2), the Assessing Officer may refer the valuation of such property to a Valuation Officer as per the provisions of Sec 50C and 155(15) will apply for valuation of capital asset.

5.7.4 Any property, **other than immovable property-**

- **without consideration**, the **aggregate fair market value of which exceeds Rs. 50,000**, the whole of the aggregate fair market value of such property; or
- **for a consideration which is less than the aggregate fair market value** of the property by an amount exceeding Rs 50,000, the aggregate fair market value of such property as exceeds such consideration.

5.7.5 Exceptions:

The provisions will not apply to any sum of money or 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; or
- (e) from any local authority defined in S 10 [20] - Explanation
- (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 S. 10 (23C); or
- (g) from any trust or institution registered u/s 12AA

5.7.3 Meaning of Property:

Property” means the following capital asset of the assessee: —

- a. immovable property being land or building or both;
- b. shares and securities;
- c. jewellery;
- d. archaeological collections;
- e. drawings;
- f. paintings;
- g. sculptures;
- h. any work of art; or
- i. Bullion

5.7.4 Meaning of Relative

Relative “means:

- I. In relation to an Individual :
 - 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 the 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 persons referred to in (2) to (6) above.

RELATIVE OF A OR MRS. A		
Spouse	Mrs. A	A
Siblings	A's brother	Mrs. A 's Brother
	A's sister	Mrs. A's sister
Lineal Ascendants – paternal	A's Parents	Mrs. A's Parents
	A's grandparents	Mrs. A's grandparents
Lineal Descendants Paternal	A's sons	Mrs. A's sons
	A's daughters	Mrs. A's daughters
	A's grandsons	Mrs. A's grandsons

Siblings of parents of Individual (Not of Spouse) Mother's brothers / sister + Father's brother / sister
Spouses of All the above persons

II. In relation a Hindu Undivided Family any member thereof.

5.7.5. Cost of Acquisition

While computing capital gains, cost of acquisition of a property received by a transferor from any exempted mode of transfer e.g. will, is taken at the same cost as that of the previous owner. Further, cost of acquisition of a property received without consideration and is chargeable u/s 56 when it is subsequently sold or transferred shall be the value considered u/s 56.

Illustration -8

A painting valued at Rs 5 lakh is transferred for Rs 3 lakh. Difference of between the consideration and the fair market value of Rs 2 lakh, will be charged u/s 56 being value of inadequate consideration. The painting is resold for Rs 10 lakh, the capital gain will be computed by taking the cost of acquisition of Rs 5 lakh i.e. Rs 10 lakh – 5 lakh = 5 lakh .

5.8. Issue of shares at premium

Aggregate consideration received by a closely held company (private company), which issues shares at premium or above their face value during a previous year to any person being a resident, to the extent such consideration exceeds the fair market value of the shares by Rs 50,000 except when the shares are issued

- to a venture capital company or
- other company notified by the Central government.

Fair market value of the shares will be determined as per the prescribed rules, i.e. net asset value or break-up value method or any other method as may be substantiated by the company to the satisfaction of the Assessing Officer, based on the value, on the date of issue of shares, of its assets, including intangible assets, being goodwill, know-how, patents, copyrights, trademarks, licences, franchises or any other business or commercial rights of similar nature.

Illustration -9

Fair market value of a company's share is Rs 100 per share. It issues 1000 shares for Rs 800 per share, then $1000 \times (800 - 100)$ = Rs 7 lakh will be treated as "income from other sources, unless the company is a venture fund or other notified company.

Following table summarizes the position of gifts u/s56

TAXABLE GIFTS AT A GLANCE		
INDIVIDUALS AND HUFs		
RECEIPTS WITHOUT CONSIDERATION		
Cash	50,001	Aggregate
Movable Assets	50,001	Aggregate
Immovable Assets	50,001	Per Property
INADEQUATE CONSIDERATION [FMV- CONSIDERATION]		
Movable Assets	50,001	Aggregate
Immovable Assets	50,001	Per Property
Shares Of Pvt Co.	50,001	Consideration or
Recd by firm or Co		difference with FMV
Sh. Premium by Pvt Co	50,001	Difference with FMV

Important Points:

1. Limit of Rs. 50,000 is for each category in case of cash and movable assets and cash but Rs. 50,000 is per immovable property as the section says "such property"
2. Rs. 50,000 is not the basic limit. Once the limit of Rs 50,000 exceeds, entire sum will be taxable. For instance, A receives cash gift of Rs 40,000 it will be exempt as it is below Rs 50,000. If he receives another gift of Rs. 10,100 from C. The aggregate gifts of Rs 50,100 will be taxable without any basic exemption.
3. The list of relatives **does not include nephews/nieces/ cousins.**
4. List of relatives includes Spouses, Siblings - own, spouses' and parents, lineal ascendants and descendants and spouses.
5. List of relatives includes uncles and aunts of the individual but not those of the spouse.
6. Stamp duty valuation will have same meaning as in S 50C.
7. Fair Market Value can be determined by the valuer.
8. Business assets like stock are not covered by these provisions and normal sale or purchase transactions will not attract the provisions of this section.
9. Any movable property like shares, securities, jewellery, drawings, paintings, sculptures, work of art or archaeological collections or immovable, without consideration, having aggregate fair market value exceeding Rs 50,000 during a previous year, for a consideration falling short of their aggregate fair market value by more than Rs 50,000 will be covered by this provision.

Illustration 10:

Compute the total income of XYZ, who receives Rs 60,000 in cash and of 1000 shares of a company valued at Rs. 40 per share as gift from each of the following persons:

1. B, his neighbour.
2. C, employer
3. D, one of his patients
4. E, his sister on the occasion of his daughter's marriage.
5. F, in contemplation of death.
6. Mrs. A
7. Mr. husband of E
8. H, son of E
9. X, a stranger on his marriage.

Solution**COMPUTATION OF TOTAL INCOME OF XYZ**

Particulars	Rupees
Salaries : Gift from employer. u/s 17	1,00,000
Profits and gains of business & profession- Gift from patient D u/s 28	1,00,000
Income from Other sources- Sec 56 sister E 's son [nephew not exempted] B- his neighbour	2,00,000
Total income	3,00,000

- Gift of shares of Rs 40,000 and cash Rs 60,000 each treated at par. Therefore, total gift in each case Rs 1,00,000
- Exempt gifts from – (with reason in brief)
 E - sister – Relative
 F in contemplation of death (Gift *mortis Causa*)
 Mrs. A- spouse –Relative
 G -E's husband – Sister's spouse –Relative
 On Occasion of marriage (Relationship not relevant)

5.9 Gifts Received by firms and companies

When a firm or a closely held company receives, in any previous year, from any person or persons, any shares of another closely held company-

- Without consideration and the aggregate fair value of such shares exceeds Rs 50,000, the whole of the aggregate fair market value of such shares or property;
- for a consideration which is less than the aggregate fair market value of the shares by an amount exceeding Rs

50,000, the aggregate fair market value of such property as exceeds such consideration .

This section will not however apply to transactions not regarded as transfer u/s 47.

5.10. Under the new sub-section 56(2)(vii), firms, widely held companies and AOP are liable to pay tax on the difference between fair market value and the actual consideration of movable or immovable asset.

Illustration-11:

A Pvt. Ltd. Buys shares in B Ltd of Rs 5 lakhs for Rs 1 lakh from C. the difference in the consideration and the fair market value amounting to Rs 4 lakhs will be taxable u/s 56.

A. Important points :

- i. The limit of Rs 50,000 is for each category.
- ii. Rs 50,000 is not the basic limit. Once the limit of Rs 50,000 exceeds, entire sum will be taxable. For instance, cash gift of Rs 45,000 received by A, is not taxable being below Rs 50,000. A receives another gift of Rs. 5,100 from C, then the aggregate gifts of Rs 50,100 will be taxable without any basic exemption.
- iii. The limit of Rs. 50,000 is per immovable property.
- iv. The list of relatives excludes nephews/nieces/ cousins.
- v. List of relatives includes spouses, own siblings, spouses' siblings and parents' siblings, lineal ascendants, descendants and their spouses.
- vi. Stamp duty valuation has the same meaning as in Sec. 50C.
- vii. Fair Market Value can be determined by the valuers.
- viii. Business assets like stock are outside the scope of this section. Hence, normal transaction of sale and purchase of goods or stocks will not attract the provisions of this section.
- ix. Any movable property like shares, securities, jewellery, drawings, paintings, sculptures, work of art or archaeological collections, without consideration the fair market value of which exceeds Rs 50,000 in aggregate during a previous year, or for a consideration falling short of their aggregate fair market value by more than Rs 50,000 will be covered by this provision.
- x. Partition in HUF, transaction between relatives and trusts are still excluded from the scope of the section.

- xi. Shares received by an individual or HUF as a consequence of demerger or amalgamation of a company or a business reorganisation of a co-operative bank shall not be subject to tax by virtue of section 56(2) (vii).
- xii. Scope of the section has been enlarged to include firms and companies in its purview.

5.10. Additional compensation

Income by way of interest received on compensation or on enhanced compensation referred to in clause (b) of section 145A.

6. DEDUCTIONS - SECTION 57

Section 57 allows the following deductions in computing the income from other sources:

I In case of taxable dividend income and interest from securities:

Any reasonable sum paid by way of remuneration or commission for the purpose of realising such income including interest on borrowed capital if such borrowed capital is used for making investment in shares or securities.

II In case of income from plant, machinery or furniture given out on hire:

- a. Current repairs to building.
- b. Current repairs to machinery, plant or furniture.
- c. Insurance premium paid for insuring the plant, machinery, building or furniture.
- d. Depreciation on building, machinery, plant or furniture.
- e. Any expenditure (not being capital expenditure or personal expenditure) which has been incurred wholly, necessarily and exclusively for earning income, such expenditure will also be allowed as a deduction, e.g. sub-letting expenses. Office stationery, rent, salaries, etc where maintenance of office is necessary for earning the income.

III In case of family pension received by legal heirs of an employee,

A standard deduction of 1/3rd of such amount received as family pension or Rs. 15,000, whichever is less.

For this purpose, family pension means a regular monthly payment made to the legal heirs of the employee after his death. Significantly, pension amount received during the lifetime of employee is taxable as salaries and not entitled to standard deduction.

IV. Employees' contribution to Provident or any other fund if deposited before the due date.

V. Any allowances paid for breeding or maintaining the racehorses.

VI. A deduction of 50% against the enhanced compensation received and no further deduction will be allowed from the income.

7. AMOUNTS NOT DEDUCTIBLE- S. 58

The following amounts are not deductible while computing income under the head "income from other source":-

- Personal expenses of the assessee;
- Any interest which payable outside India, on which income tax has not been paid or deducted at source;
- Any sum paid on account of wealth tax in India or abroad;
- Any amount not allowable by virtue of it being unreasonable;
- In case of foreign companies, expenditure in respect of royalties and technical services received under an agreement made after 31/3/76; and
- Any expenditure in connection with income from winning from lotteries, crosswords, puzzles, races including racehorses, car races and other games of races, gambling, betting of any form. However, expenses are allowed as a deduction in computing the income of an assessee who earns income from maintaining as well as holding racehorses.

8. MISCELLANEOUS

a) Balancing charge taxable-S. 59

Any amount received or benefit derived in respect of any expenditure, incurred or loss or trading liability allowed shall be deemed to be the income of the year in which such benefits is accrued or received as the case may be.

b) Method of accounting- S. 145

Section 145 relating to method of accounting is also applicable to the computation of income from other sources. Income under this head is computed in accordance with the method of accounting regularly employed by the assessee i.e. if the assessee accounts only on cash receipt and cash payment basis, income will be treated on cash payment and cash receipt basis only; otherwise it will be treated on mercantile basis. An assessee can adopt either the cash method or accrual method of accounting. Hybrid method is not permissible. However, certain items like lottery, horse races,

dividend u/s 2(22)(e) can only be recorded on cash basis because of their variable nature.

c) Grossing Up:

Many times, dividends, interest from securities are received after TDS. In such case amount to be included in total income is gross amount and not the amount received. Amount of TDS should be added back.

Illustration- 3.

A receives taxable interest of Rs. 18,000 after deduction of 10% TDS . Find out the taxable income.

Solution

Since TDS is 10%,

Net amount will be 90%

Amounts to be taxed will be gross amount Rs 20,000 i.e.

$$\frac{\text{Rs } 18,000 \times 100}{90}$$

Rupees 20,000 will be included in the income and credit for TDS of Rs. 2,000 will be claimed against the tax payable.

9. SELF-EXAMINATION QUESTIONS:

- 1) Enumerate any five items of income, which are included under the head 'income from other sources'.
- 2) Define Dividend. Discuss the taxability of dividend.
- 3) What are the incomes included under the subhead of winning? What is the rate of tax on such incomes?
- 4) What are the deductions allowable in respect of hire charges of plant and machinery?
- 5) Are there any amounts, which are not allowed as deductions while computing the income from other sources? Give examples.
- 6) A is in receipt of pension as a retired government employee @ Rs. 10,000 per month. Besides, he is in receipt of family pension of his late wife @ Rs. 6,000 per month. Show how the two amounts will be treated for tax purposes.
(Own pension salary / wife's pension other sources with std. deduction Rs. 15000)
- 7) Show the head of income under which the following items would be charged.
 - a. Rent received by an event manager on letting out tents /pandal.
 - b. Hiring charges received by a taxi driver.

- c. Car hiring charges received by a company from the cars requisitioned by the Election Commission
- d. Interest on Income Tax Refund
- e. Rent received by letting out own house and
- f. Rent received by sub-letting premises.
- g. Computer hiring charges.
- h. Salary of director
- i. Salary of M.P/ MLA
- j. Rent of a house.
- k. Rent of a plot of land.
- l. Rent of a machine let on hire along with building and letting is separable.
- m. Dividend from domestic company.
- n. Winning from TV game show like.

(Hints/Answers: item e/j remaining other sources. Director if employee, then salary)



EXCLUSIONS AND DEDUCTIONS

Synopsis:

1. Introduction and Objectives
2. Exemptions and deductions
3. Income exempt under section 10
 - a. Agricultural income-S10(1)
 - b. Receipts by a member from a Hindu Undivided Family-S 10(2)
 - c. Share of profit of a partner in a firm –S10(2A)
 - d. Income of minor Child –S.10(32)
 - e. Dividend Income –domestic companies-S10(34)
 - f. Dividend Income- Mutual fund units- S10(35)
 - g. Other Exemptions
4. Deductions –S.80 –Chapter VIA
 - a. Investments –S80C
 - b. Pension Plan –S 80CCF
 - c. Mediciam -80D,
 - d. Physical Disability -80DD,
 - e. Treatment f major diseases -80DDB,
 - f. Interest on educational Loans 80E,
 - g. Physical Disability(Own)-80U:
5. Solved Examples
6. Self-Assessment questions

1. INTRODUCTION & OBJECTIVES

Some incomes are not chargeable under the Income Tax Act 1961. This is done two ways namely – some incomes are not included in the total income and some incomes are taken into consideration for computing the total income, but deduction is allowed in respect of such income under section 80 of chapter VIA of the Act. This lesson deals with the provisions of Income Tax Act 1961 relating to exemptions and deductions.

2. EXCLUSIONS VS DEDUCTIONS

2.1. Exclusions:

Income, which is not chargeable to income tax, is called exempt income. Hence, such incomes are excluded from the computation of total income and do not form part of total income

Every income is chargeable to income tax unless it is specifically exempt and the person, who claims an income to be exempt, has to prove that such receipt is so exempt.

Exemptions are granted to a person or class of persons e.g., charitable trusts in respect all or some of their incomes. On the other hand, some incomes are e.g., agricultural income exempt in the hands of all types of assesseees. Further, exemptions may be unconditional or subject to fulfillment of certain condition such as in case of startups, SEZ etc.

Sections 10 to 13 deal exclusively with incomes, which are exempt from income tax while sections 15 to 56 provide for certain exemptions available under a particular head while computing income under different heads viz Salaries, Income from house property, Profits and gains of business & profession, Capital gains and Income from other sources.

A receipt not falling under the definition of income u/s 2(14) or a receipt, which is of capital nature, may be claimed as exempt, unless it is specifically chargeable to income tax.

To summarize exempt incomes may be of following types:

- Income exempt u/s 10-13
- Income exempted under different heads of income S 15-56
- Income of capital nature not specifically chargeable to income tax and
- Income not falling in the definition of income.

2.2 Deductions

After the income has been computed under different heads of income as provided in sections 15-56, deductions are allowed under the provisions of sections 80 of chapter VIA of the Act. Hence, deductions are allowed after the gross total income is computed either in respect of any income or revenue or in respect of any payment or expenditure.

Sections 80IA, 80IB etc. provide for deduction in respect of revenue or income of a class of assesseees like software, infrastructure companies, companies engaged in construction of affordable housing etc., while sections 80 C, 80D etc. provide for

deductions in respect of investments in specified securities, payment of mediclaim, expense on handicapped dependent etc.

Some important exemptions and deduction are discussed below.

3. INCOME EXEMPT UNDER SECTION 10:

Section 10 provides that any income falling within any of the clauses of that section shall not be included in computing the total income of a previous year of any person. However, burden is on the assessee to prove that a particular item of income falls within this section.

Following exempt incomes (covered in syllabus) are discussed as under:-

3.1 AGRICULTURAL INCOME – S 10(1):

Under the constitution of India, agriculture is in the state list and the central government is not constitutionally competent to levy taxes on agriculture. Accordingly, agricultural income is exempt u/s 10(1) of the Act. However, for rate purposes the agricultural income is considered if it exceeds Rs. 500.

Meaning of agricultural income

U/s 2(1A) Agricultural income” means any :-

- A. any **rent or revenue** derived from land-
 - which is situated in India and
 - is used for agricultural purposes
- B. any **income derived from such land** by
 - agriculture; or
 - raising the performance by a cultivator or receiver of rent-in-kind of any process to render the produce raised or received by him fit to be taken to market or
 - the sale of such produce without performing any other process as stated above. ;
- C. **any income derived from any building :**
 - Owned and occupied by owned and occupied by the
 - i. receiver of the rent or revenue of any such land, or
 - ii. cultivator or
 - iii. receiver of rent-in-kind, of any such land
 - iv. If such building is
 - a) on or in the immediate vicinity of the land, and

b) required as a dwelling house, or storehouse, or other outbuilding by reason of its connection with the land, and the land is

- assessed to land revenue in India or
- subject to local rates and taxes assessed and collected by the government and
- situated in any area within the distance measured aerially from the local limits of any municipality or cantonment board depending upon its population as per the last published census namely -
 - 2 kms if population is more than 10,000 but not exceeding 1 lakh;
 - 6 kms. if population is more than 1 lakh but not exceeding 10 lakh; or
 - 8 kms. if population is more than 10 lakh.

Other Points

1. Income from land situated in urban area is not exempt
2. Land situated in areas having population of 10,000 or less will qualify for exemption.
3. Agricultural income must be received in India.
4. Agricultural income from a foreign country is treated as non-agricultural income in India.
5. Receipts arising on transfer of agricultural land u/s 2(14) is not considered agricultural income
6. Any income arising from letting out the building for residential or business purpose other than agriculture will not be agricultural income

Illustration 1

Tukaram employs Sakham to carry out agriculture on his agricultural land at a remuneration based on the value of agricultural produce. Sakham remits the sale proceeds of the agricultural produce to Tukaram after deducting his share of remuneration. Discuss the tax liability of Tukaram and Sakham.

Solution

Income on sale of agricultural produce derived from agricultural in India is agricultural income is exempt u/s 10(1) in the hands of Tukaram.

However, Sakham gets salary for rendering his services. Salary income is not derived from agricultural land; hence, it will be chargeable to income tax under the head "Salaries".

3.2 Receipts by a member from a HUF-Sec 10(2)

Section 10(2) provides that any sum received by an individual as a member of a Hindu undivided family either out of income of the family or out of income of impartible estate belonging to the family will be exempt from tax.

A Hindu Undivided family (HUF) is a separate and independent entity liable to pay tax on its income. Hence, when its income is distributed among its members, there will be no further tax liability as it will amount to taxing the same income twice.

This is subject to an exception. When a member of the family converts his personal property into the family property (called as throwing self-property into family hotchpot), then the income derived from such converted property will not be eligible for exemption u/s 10(2). Instead, it will be clubbed u/s 64 (2), in the hands of the member, who has transferred the property to the family.

Illustration 2

X, an individual, has personal income of Rs. 5,00,000. He is also a member of a Hindu undivided family, which has an income of Rs. 2,50,000. Out of income of the family, X gets Rs. 1,25,000, as his share in the income of the family. Show the status of the income from taxability point of view.

Solution:

X is liable to pay tax only on his personal income of Rs. 5,00,000. His share of Rs. 1,25,000 from HUF is exempt in the hands of X under section 10(2) irrespective of the fact whether the family is chargeable to tax or not. The HUF is liable to tax in respect of its income of Rs. 2,50,000.

3.3 Share of Profit of a partner in a firm –Sec. 10(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 will be exempt from tax u/s 10(2A). Since, a firm like a HUF is assessed as a separate entity, this exemption is provided to avoid double taxation of same income first in the hands of the firm and then again in the hands of the partners.

However, any remuneration paid by the firm or any interest on capital shall not form part of the share of profit received by partner and will be taxed in the hands of the partners to the extent it was allowed as a deduction to the firm and will be taxed in the hands of the partners. But any remuneration or interest on capital in excess of the limits laid down in section 40 shall be chargeable to tax in the assessment of the firm and will form the part of the income allocated to partners exempt u/s 10(2A).

3.4 Income of minor child-S10(32):

Under 64(1A), income of a minor child is clubbed in the hands of his parent, who is having higher income except income earned by minor's personal efforts or skill. Section 10(32) provides for an exemption of the amount included in the income of such parent subject to a maximum of Rs. 1,500 per child.

Illustration 3

What will be the amount exempted U/s 10(32) if income of Rs 1,000 of Suresh, a minor son is included in the income of his father Sudesh.

Solution

Exemption u/s 10(32) is equal to actual income included in the hands of parent or Rs. 1,500, whichever is less. Hence Exemption available to u/s 10 (32) will be Rs. 1000 only.

Illustration 4

In the illustration 3, what will be the amount exempted U/s 10(32) if income of Suresh is Rs 15,000.

Solution

Exemption U/s 10(32) is equal to actual income included in the hands of parent or Rs. 1,500, whichever is less. Hence exemption available to u/s 10 (32) will be Rs. 1,500 only

Illustration 5

What will be the amount of deduction U/s 10(32) if Incomes of Ashok and Babu amounting Rs 7,500 and Rs 5,500 were clubbed with the income of their father Chandu.

Solution

Chandu will get exemption of Rs 3,000 being Rs 1,500 per child.

3.5 Dividend from domestic companies–S 10(34)

Any dividend declared by a domestic company which is liable for dividend distribution tax @ 15% covered by section 115-O is exempt under section 10(34) and hence would not be chargeable to tax. With effect from A.Y. 2018-19, the tax on deemed dividend covered in S 2(22)(e) is included in distribution of profit u/s 115-O with tax of 30%. Hence, such deemed dividend will also be eligible for exemption under this section

This exemption is subject to the newly inserted section 115BBDDA, which provides that any income by way of aggregate dividend in excess of Rs. 10 lakh shall be chargeable to tax in the case of an individual, Hindu undivided family (HUF) or a firm who is resident in India, @ 10%. Of gross dividend in excess Rs. 10 lakh. No deduction in respect of any expenditure or allowance or set-off

of loss shall be allowed to the assessee in computing the income by way of dividends

3.6 Dividend from Units of mutual funds –S 10(34)

Dividend or income received in respect of units of mutual fund or administrator of the specified undertaking or specified company is also exempt from Income tax under section 10 (34). However, the income does not include income on transfer of such units.

3.7 Other Exemptions:

Sec. 10 provides a comprehensive list of exempt incomes. Important exemptions e.g. gratuity, pension etc., which are for computation of income under the five heads of income, are incorporated at appropriate lessons dealing with such heads of income. *Remaining exemptions, though not directly covered by the syllabus, may have a bearing on the computation.* A brief summary of such exemptions is given in the following Appendix

APPENDIX

A. EXEMPTION TO FOREIGNERS/ NON RESIDENTS.

1. Interest income of non-resident (persons of Indian origin) from notified securities, saving certificates/ NRE Account. Purchased in convertible foreign exchange—Sec 10(4).
2. Remuneration / salary of
 - a) Foreign diplomats -Sec 10(6).
 - b) a trainee of a foreign government-Sec 10(6)(xi),
 - c) a foreign national as an employee of foreign Enterprise I – Sec 10(6)(vi)
 - d) Non-Resident Employee of a Foreign Ship—Sec 10(6)(viii)
 - e) Person from a foreign government under Co-operative Technical Assistance Programme/ projects Sec. 10(8)
 - f) a consultant under Grant Agreement between the International Organisation and the Government of Foreign State- Sec .10(8A) :
 - g) non-resident, engaged by the agency for rendering technical services in India in connection with any technical assistance programme or project, provided in accordance with an approved agreement - S. 10(8A)
 - h) 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 - Sec

.10(8A)

- i) an individual who is assigned to duties in India in connection with any technical assistance programme and project from a consultant referred to S 10(8A), income-S. 10(8B)
- 3. Income other than salary, royalty or fees for technical services from Government or an Indian concern under an approved agreement and if their tax liability is paid by the employer the tax so paid is exempt from tax. - Sec 10(6B)
- 4. Income accruing or arising outside India by any family member of persons covered u/s 10 (8),(8A) or (8B) , in respect of which such member is required to pay any income tax or social security tax to the Government of that foreign state. –Sec 10(9)
- 5. Amount of tax actually paid by an employer, at his option, on non-monetary perquisites on behalf of an employee in the hands of the employee. Sec – 10(10CC).

B. EXEMPTION TO SALARIED EMPLOYEES

Exemption granted to salaried employee have been dealt in detail in the lesson relating to salaries such as

- a) Value of any travel concession/ assistance-S.- 10(5),
- b) allowance paid by the government to a Indian citizen rendering service outside India -Sec10 (7)
- c) Death cum Retirement gratuity -Sec-10(10)
- d) Commuted pension10 (10A),
- e) Leave encashment Sec 10 (10AA)
- f) Retrenchment compensation -Sec 10(10B)
- g) Voluntary Retirement Compensation of -Sec 10(10C)
- h) Value of tax-paid perquisite -10(10CC)
- i) leave travel allowance,
- j) Payment from statutory PF -Sec10(11)
- k) Any payment from National Pension Trust or upto 40% on closure of such account -Sec 10(12A /12B)
- l) house rent allowance 10(13A),
- m) special allowances etc. 10(14). Etc.

C. EXEMPTIONS TO INSTITUTIONS / FUNDS :

The income of the following institutions is exempt subject to certain conditions:

1. Local authority i.e. a panchayat, municipality, municipal committee, district board or cantonment board.- S. 10(20)
2. Approved Notified scientific and research association applying which has as its object, undertaking research in social science or statistical research, and applying its income wholly and exclusively to its objects, including profits and gains of a business carried on by an institution, which is incidental to its objects. - S. 10(21)
3. News agency set up in India which 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.- S. 10(22B)
4. Regimental Fund or non-public fund.- S. 10(23AA)
5. Approved fund for the welfare of employees.- S. 10(23AAA)
6. Pension fund (Jeevan Suraksha) set up by the Life Insurance Corporation of India or a pension fund of any other insurance company.- S. 10(23AAB)
7. Khadi and Village industries Board.- S. 10(23B)
8. Public charitable trusts , religious institutions and political trusts -Sec. 11 ,12, 13
9. European Economic Community.
10. SAARC Fund for Regional Projects.
11. ASOSAI-Secretariat
12. Insurance Regulatory and Development Authority
13. Prime Minister's Relief Fund
14. National Foundation for Communal Harmony
15. University/educational institution, hospital or medical institution 10 (22)/(22A)
16. Professional bodies. S. 10(23A)
17. Notified fund, charitable/ religious institution or trust.- Sec 10(22B)
18. Mutual fund - S. 10(22B)
19. Notified Investor Protection Fund set up by recognised Stock Exchanges
20. Credit Guarantee Fund Trust for Small Industries
21. Approved Venture Capital Fund or Venture Capital Company-10(23FB)
22. Prasad Bharati (Broadcasting Corporation of India) S.10(23BBH)

23. Swachh Bharat Kosh – S . 10(23C(iiaa))
 24. Clean Ganga Fund - S . 10(23C(iiiaa))
 25. Core Settlement Guarantee Fund set up by a recognized clearing corporation in accordance with notified regulations- S 10(23EE) to the extent of contributions from members fines and income from investments.
 26. Trade Union or Association of trade Unions from house property and other sources.- S. 10(24)
 27. Statutory Provident Fund under P. F. Fund Act.- S. 10(25)
 28. Employees' State Insurance Fund set up under the ESI Act- S. 10(25A)
 29. Members of scheduled tribes residing in specified areas. - S. 10(26)
 30. Statutory Corporation, body, association or institution formed or established for promoting the interests of the members of Scheduled Castes/ Scheduled Tribes or backward classes or of any two or all of them.- S. 10(26B)
 31. Corporation established by the Central/ State Government for promoting the interests of a notified minority community. - S. 10(26BB)
 32. Ex-Servicemen Corporation established under an Act for the welfare and economic upliftment of ex-servicemen being the citizens of India.- 10(26BBB)
 33. Co-operative Society formed for promoting the interest of members of either the Scheduled Caste or Scheduled Tribes.- S. 10(27)
 34. Coffee Board, Rubber Board, Tea Board, Tobacco Board, Marine Products Export Development Authority, Agricultural and Processed Food Products Export Development Authority and Spice Board.- S. 10(29A)
 35. Subsidy received from the Tea Board for replantation or replacement of tea bushes or for rejuvenation or consolidation of areas used for cultivation of tea under any scheme notified by the Central Government-. S. 10(30)
 36. Subsidy received from the Rubber Board, Coffee Board, Spices Board or any other Board under any scheme of replanting or replacement, etc.- S. 10(31)
- Exemptions not be available to the institutions u/s 10(23C) having commercial receipts of Rs. 25,00,000 or more

D. CAPITAL GAINS

1. Any long-term capital gain arising on transfer of eligible equity shares of a company acquired on or after 1.3.2003

but before 1.3.2004 and held for 12 months or more if STT is paid except in case of a transaction undertaken in foreign currency on a recognised stock exchange located in an International Financial Services Centre.

2. Any long-term capital gains from transfer of equity shares of a company or units of an equity-oriented fund on or after 1.10.2004 and subject to Securities Transaction Tax -Sec 10(38).
3. Any capital gain arising to an individual/ HUF on compulsory acquisition of an agricultural land in urban areas (situated within the jurisdiction of a municipality or a cantonment board having population of 10,000 or more or within 8 Kms from the local limits of such municipality/ board), where the compensation/ consideration is received by the assessee on or after 1.4.2004. Provided, the land was being used for agricultural purposes by the HUF/ individual or his parent(s), during the period of 2 years immediately before acquisition.
4. Any income arising from the transfer of a US 64 subject to the condition that any loss arising on transfer of units of US.64 cannot be set off against any income in the same year in which it is incurred and the same cannot be carried forward—Sec 10(33.)

E. MISCELLANEOUS

1. Daily allowance of Members of Parliament while the parliament is in session is and Members of State Legislative Assemblies (upto Rs. 2000) - Sec 10(17)
2. Any sum received on life insurance policy (including bonus) not being the amount received on the following policies -
 - a. any sum received u/s 80DD (3) or 80DDA (3);
 - b. any sum received under a Keyman insurance policy;
 - c. any sum received under an insurance policy (issued after March 31, 2003) in respect of which the premium payable for any of the years during the term of policy, exceeds 20 per cent of the actual sum assured except in case of the death of the person and the value of any premiums agreed to be returned or of any benefit by way of bonus or otherwise, over and above the sum actually assured, which is received under the policy by any person, which shall not be taken into account for the purpose of calculating the actual capital sum assured under this clause. -Sec 10(10D),
3. Family pension received by the widow or children or nominated heirs of a member of the armed forces or paramilitary forces of the Union is not chargeable to tax from A.Y. 2005-06, if death is occurred in such circumstances given below—

- a. acts of violence or kidnapping or attacks by terrorists or anti-social elements;
 - b. action against extremists or anti-social elements;
 - c. enemy action in the international war;
 - d. action during deployment with a peace keeping mission abroad;
 - e. border skirmishes;
 - f. laying or clearance of mines including enemy mines as also mine sweeping operations;
 - g. explosions of mines while laying operationally oriented mine-fields or lifting or negotiation mine-fields laid by the enemy or own forces in operational areas near international borders or the line of control;
 - h. in the aid of civil power in dealing with natural calamities and rescue operations; and
 - i. in the aid of civil power in quelling agitation or riots or revolts by demonstrators. - Sec 10(19),
4. Any income by way of dividend referred to in section 115-O from a domestic company or any income in respect of units of mutual fund; UTI, from the administrator units from the specified company is exempt under section 10(34)/ (35),
5. Interest income arising to certain persons [Section 10(15)]:
- (i) Income by way of interest, premium on redemption or other payment on notified securities, bonds, annuity certificates or other savings certificates is exempt subject to such conditions and limits.
- Interest from Post Office Savings Bank Account:
- (1) Rs. 3,500 in case of an individual account.
 - (2) Rs. 7,000 in case of a joint account.
- Interest on deposit certificates issued under the Gold Monetization Scheme, 2015 Section
6. U/s 10AA export incomes of undertakings in SEZ are exempt on pro rata basis i.e.
- $$\frac{\text{Business Profit X Export Turnover}}{\text{Total Turnover}}$$
7. Incomes of charitable trusts and political parties subject to the provisions of Sec 11, 12 and 13.
8. any income of a foreign company received in India in Indian

currency on account of sale of crude oil to any person in India subject to approved conditions being satisfied received under a notified agreement or an arrangement with the Central Government or approved by it and the receipt of the money is the only activity carried out by the foreign company in India

9. Section 10(48A): Exemption of income accruing or arising to a foreign company on account of storage of crude oil in a facility in India and sale of crude oil therefrom to any person resident in India. if (1) such storage and sale by the foreign company is pursuant to an agreement or an arrangement entered into by the Central Government or approved by the Central Government; and (2) having regard to the national interest, the foreign company and the agreement or arrangement are notified by the Central Government in this behalf.
10. section 10(48A) If the premium payable during any previous year for a policy issued on or after 1.4.2012 exceeds 10% of the actual capital sum assured, the entire amount received under such policy shall be taxable except when the sum received on the death of a person

4. DEDUCTIONS UNDER CHAPTER VI A

4.1 Sections 80A and 80AB of chapter VIA provide for a basic framework for deduction to be made from gross total income. Salient points of such framework are as under:-

- (a) Aggregate of total income of an assessee will be computed under different heads of income as provided in sections 15-58 before making any deduction under this chapter called the gross total income.
- (b) From the gross total income long term capital gains, short term capital gain under winnings from lottery, crossword puzzles etc. are excluded as these items are treated differently for tax purposes.
- (c) From the gross total income, deductions are allowable under sections 80C to 80U of chapter VIA.
- (d) The aggregate of all deductions under this chapter cannot exceed the amount of gross total income of the assessee.
- (e) Deduction is admissible to the members of an AOP or BOI in relation to their share therein under sections 80G, 80GGA, 80GGC, 80HHA, 80HHB, 80HHC, 80HHD, 80I, 80IB, 80IC, 80ID, 80IE, 80J or 80JJA.

(f) No deduction will be allowed if any exemption is claimed and allowed to eligible assessee, enterprises, units, or undertakings under sections 10A, 10Aa, 10B, 10BA, or 35AD for that year. Further, such deduction shall not exceed the profits and gains of such undertaking or unit or enterprise or eligible business.

(g) As per section 80A, the above deduction will be available only if the assessee makes a claim in his return of income.

(h) Section 80B clarifies that deduction in respect of any income shall be allowed if such income is included in gross total income.

(i) For deduction in respect of any payment, the assessee has to claim the deduction and submit gives the proof of such for any investments/ expenditure etc.

(j) Deductions under Chapter VIA are of three types:

- I. In respect of expenditure or investments made by the assessee - section 80C to 80G
- II. In respect certain income - sections 80HH to 80RRB
- III. irrespective of whether income or expenditure- Sec 80 U allowable to a handicapped person.

Some of the deductions covered by the syllabus are discussed in the following paragraphs.

4.2 Deduction in respect of investments in specified saving schemes-section 80C:

Section 80C provides for deduction in respect of investment or contribution towards specified saving schemes. The basic scheme of the section is as follows:

(i) Only individuals and HUFs are eligible for deduction under this section. Other assesseees are not eligible for deduction u/s 80C.

(ii) Both residents and the non-resident assessee are eligible for the deduction under the section

(iii) The deduction is allowed in respect of the aggregate amount **paid or deposited** during the previous year by the assessee in eligible saving schemes.

(iv) The aggregate amount paid or deposited towards these schemes is called **Gross Qualifying Amount**.

(v) The payments/investments eligible under this section are:

(a) Life insurance premium paid on a policy taken or renewed by

- An individual
 - on his own life,

- life of the spouse or any child
- child may be dependent or independent
- A Hindu undivided family on the life of any member of the family

The premium including the arrears of premium should not exceed 10% of sum assured if policy taken after 0-1-04-2013 (15% for persons with handicap u/s 80U or person suffering from serious disease u/s 80DDB on policy taken after 01-04-2014). Prior to this, the restriction was up to 20% for all assessees.

- (b) Any sum paid under the contract of non –commutable deferred annuity plan for the purpose of securing the individual or his spouse or children to pay a deferred annuity
- (c) Any sum deducted from salary payable to a Government employee for the purpose of securing the individual or his spouse or children to pay a deferred annuity subject to a maximum of 20% of salary;
- (d) Contribution towards statutory provident fund;
- (e) Contribution towards 15 year Public provident fund(PPF) in the name of himself, wife or child or a family member upto a maximum of Rs 1,00,000;
- (f) Contribution towards Recognized provident fund;
- (g) Contribution towards an approved *Superannuation Fund*;
- (h) Investment in 10 / 15 years Post office cumulative term deposits(CTDS);
- (i) Subscription to notified deposit scheme e.g. NSS
- (j) Subscription to National savings certificates, VIII Issue
- (k) Contribution for participating in the Unit-linked insurance plan (**ULIP**) of Unit Trust of India;
- (l) Contribution for participating in the Unit-linked insurance plan (**ULIP**) of LIC Mutual Fund (i.e. Dhanraksha plan of LIC Mutual Fund);
- (m) Payment for notified annuity plan of LIC (i.e. Jeevan dhara, Jeevan akshay, New jeevan dhara, etc. or any other insurer;
- (n) Subscription towards notified units of mutual fund/ UTI
- (o) Contribution to notified pension fund set up by mutual fund or UTI;
- (p) Any sum paid including accrued interest as subscription to home loan account scheme of the National Housing Bank(**NHB**);

- (q) Any sum paid as tuition fees (but not donation) to any university/college/educational Institution in India for full time education for maximum 2 children;
- (r) Any subscription towards infrastructure bonds or units of Mutual Funds;
- (s) Any amount paid for the purchase or construction of a residential house property or for purchase of land;
- (t) Term deposits for a fixed period for at least 5 years with a scheduled bank under a notified scheme;
- (u) Deposit in an account under Senior citizens savings scheme, 2004;
- (v) 5- years post office time deposit account;
- (w) Subscription to notified bonds issued by NABARD;
- (x) Subscription to eligible issues of equity shares or debentures of an Indian public company or a public financial institution where the entire proceeds of the issue is wholly and exclusively for the purposes of any business specified for developing, maintaining and operating an infrastructure facility for generation or generation and distribution of power or for providing telecommunication services whether basic or cellular or for developing, developing and operating or operating and maintaining an industrial park or a special economic zone- SEZ

Amount of deduction allowable u/s 80C will be:-

- Whole of the aggregate amount paid or deposited in the above mentioned schemes the gross qualifying amount or
- Rs 1,50,000, whichever is less.
- U/s 80CCE, maximum deduction u/s 80C, 80CCC and 80CCD cannot exceed Rs 1,50,000.

(vi) Some important points:

- Payment for house include amount paid to authorised developers or repayment of loans.
- The amount of investments need not necessarily be made out of the taxable income
- Life insurance premium paid for parents will not be allowable even if parents are dependent on the assessee.
- Life insurance premium paid for married daughter will be allowable.
- Dependence of wife or children is not necessary for claiming deduction under this section.
- Refundable premium and bonus on premium are not eligible for deduction

- Premature termination(before the period shown below) from any scheme will have the following effects:
 - In the year of termination, deduction will not be allowed ;
 - Premium earlier paid and allowed as deduction will be brought back to tax in the current year and added to the total income in the assessment year pertaining to the year of withdrawal.

Premature withdrawal/Transfer/ Termination	
Life insurance Policy	Two years for whole life policy
	One year for other policy
P/O TDS / SCSS	Five Years
Unit Linked Insurance Plan	Five Years
House property-Transfer	Five Years

Illustration 1:

A whole life policy on which a premium of Rs. 6,000 has been paid upto last year and Rs. 3000 is the current year's premium otherwise eligible for deduction u/s 80C. What will be the effect if the contract is prematurely terminated during the financial year 2017-18?

Solution

Premium paid in financial year 2017-18 will not be eligible for deduction u/s 80C and the old premium of Rs. 6000 allowed earlier will be added to the income of assessment year 2018-19.

Illustration 2

Shyam makes the following payments during the financial year 2015-16.His Gross Total Income amounts to Rs. 5,00,000 .Shyam asks you to calculate the deduction available under section 80C and the taxable income for the A.Y. 2018-19.

School fees of his 4 children	Rs 50,000
University fees of his wife	Rs 20,000
Life insurance for wife and kids	Rs 10,000
Life insurance for parents	Rs 15,000
Life insurance for father-in-law	Rs 10,000
NSC	Rs 20,000
Repayment of principal for house	Rs 35,000
Coaching class fees	Rs 11,030

Solution

Gross Total Income		Rs. 5,00,000
School fees up to 2 children	Rs 25,000	
University fees of wife - Not allowed	NIL	
Life insurance for wife and kids	Rs 10,000	
Life insurance for parent Not allowed	NIL	
Life insurance for father-in-law- Not allowed	NIL	
NSC	Rs 20,000	
Repayment of principal for house	Rs 35,000	
Coaching class fee Not allowed	NIL	
Deduction u/s 80C		Rs. 90,000
Total Income		Rs.4,10,000

Illustration 3

Ashok has a Gross Total Income of Rs 8,00,000 for the AY 2018-19. He had availed of a deduction in AY 2014-15 of Rs 7,000 in respect of a Life insurance policy, which was prematurely terminated in P.Y. 2017-18 He made the following investments for the P.Y. 2017-18

1. Insurance for himself (sum assured Rs 1,00,000) Rs. 28,000.
2. Insurance for wife (employed with MNC) Rs 25,000
3. Insurance for son but unpaid Rs 7,500
4. Compute deduction u/s 80C and the taxable income of Ashok.

Solution

Computation of total income		Rs
Gross Total Income		5,00,000
Add: Deduction of last year on termination of policy		7,000
Revised Gross Total Income		5,07,000
Insurance for himself (in excess of 20% of sum assured)	Rs 20,000	
Insurance for wife (dependence not relevant)	Rs. 25,000	
Insurance for son (not paid)	Nil	
Total deduction u/s 80C		45,000
Total Income		4,62,000

Illustration – 4

GTI of W for AY 2018--19 is Rs 12,00,000. He pays premium of Rs 22,000 on a policy on his own life for Rs 1,00,000 , Rs 10,000 each for policies of his son and brother, both being dependent on him. W also pays Rs. 20,000 for unrecognized Provident fund, Rs. 10,000 towards PPF Rs 10,000 in ULIP . He also repaid housing

loan to ICICI Bank Rs 80,000 with Rs 20,000 towards outstanding interest.

School fees of three his children amounts to Rs 4, 000 Rs. 5,000 and Rs 6,000 respectively.

Compute the deduction/s 80C and the taxable income of W

Solution

Computation of total income		Rs
Gross Total Income		12,00,000
Insurance-self (over 10% of sum assured	2,000	
Insurance(son) – dependence not relevant	10,000	
Insurance for brother not allowed	Nil	
Unrecognized Provident. Fund – Not allowed	Nil	
Public provident Fund	10,000	
Unit Linked insurance plan	10,000	
Housing loan –Principal	80,000	
School fee –2 children – Higher figures considered 6,000=+5,000	11,000	
Total deduction u/s 80C -	1,41,000	1,41,000
Total Income		10,59,000

4.3 Deduction in respect of Contribution to certain pension funds – Sec80CCC.

U/ s 80CCC, deduction is allowed to Individuals in respect of amounts paid/ deposited (excluding any interest / bonus accrued/ credited to the assessee) during the previous year to effect or keep in force a contract for any annuity plan of Life Insurance Corporation of India or any other insurer for receiving pension from the fund u/s 10(23AAB).

The amount received by the assess or his nominee a) on account of the surrender of the annuity plan whether in whole or in part, in any previous year, or (b) as pension received from the annuity plan shall be deemed to be the income of the assessee/ nominee, in the year of withdrawal or when pension is received maximum deduction u/s 80C, 80CCC and 80CCD shall not exceed Rs 1,50,000. (This section is directly not covered in syllabus but has an impact on deduction u/s 80C

4.4 Payment in respect of health insurance premia- S. 80D:

Provisions of section 80D, which provides for a deduction in respect of the health premia paid are summarized as under :--

(a) **Eligible Assessee** : individual or a Hindu undivided family

(b) **Nature of Deduction** : payment made towards medical insurance premia paid during the previous year

(c) **Mode of Payment** : The premium shall be paid by any mode other than cash, e.g. cheque, ECS or other electronic mode. However, payment for preventive health check-up may be made by any mode including cash.

(d) Amount of Deduction In case of an individual assessee

Premium and checkup for self and family

(i) Deduction shall be aggregate of the following payments made for **self and family**, or Rs 25,000, whichever is less

- a) the whole of the amount paid (premium) to effect or to keep in force an insurance on the health of the assessee or his family ;
or
- b) any contribution made to the Central Government Health Scheme or other notified scheme (popularly called Mediclaim policy), or
- c) any payment made on account of preventive health check-up of the assessee or his family upto Rs 5,000

(ii) Medical expenditure for self or family member

The whole of the amount paid on account of medical expenditure incurred on the health of the assessee or any member of his family being **a very senior citizen** if no amount has been paid to effect or to keep in force an insurance on the health of such person or Rs 30,000, whichever is less.

Thus, an assessee may either pay the insurance premium (Rs 25,000+ 5,000 for medical checkup) or incur medical expenditure subject to a maximum limit of Rs. 30,000.

(iii) Premia paid for parents

The amount of deduction shall be aggregate of the following or Rs 25,000 whichever is less

- (a) the whole of the amount paid to effect or to keep in force an insurance on the health of the parent or parents of the assessee or
- (b) any payment made on account of preventive health check-up of the parent or parents of the assessee as does not exceed Rs 5,000

(iv) Medial Expenditure for parents

The whole of the amount paid on account of medical expenditure incurred on the health of *any parent* of the assessee

being *very senior citizen not exceeding* in the aggregate Rs. 30,000 if no amount has been paid to effect or to keep in force an insurance on the health of such person

Maximum deduction under both the above cases will be restricted to Rs 30,000

(v) Other points

- '*Family*' means the spouse and the dependent children of the assessee
- "senior citizen" means an individual resident in India who is of the age of *sixty years or more* at any time during the relevant previous year;
- "very senior citizen" means an individual resident in India who is of the age of *eighty years or more* at any time during the relevant previous year.
- The parents and the spouse may not be dependent upon the assessee but his children must be dependent for claiming the deduction
- Expenses paid for preventive health check-up have a sub limit of Rs 5,000 within the overall limit of Rs 25,000 /30,000 and such expenses may be paid in cash.
- Any medical insurance premia paid to effect or keep in force an insurance on the health of any person being a senior citizen, or a very senior citizen, the limit of Rs 25,000 (for individual and HUF) will be enhanced to Rs 30,000
- Insurer should be notified by the IRDA or Central Government

(e) Amount of Deduction to A Hindu undivided family :

Where the assessee is a Hindu undivided family, amount of deduction shall be the aggregate of the following, namely:—

- (i) whole of the amount paid to effect or to keep in force an insurance on the health of any member of that Hindu undivided family as does not exceed in the aggregate Rs 25,000 ; and
- (ii) the whole of the amount paid on account of medical expenditure incurred on the health of any member of the Hindu undivided family being a very senior citizen as does not exceed in the aggregate Rs 30,000 , if no amount has been paid to effect or to keep in force an insurance on the health of such person:

The aggregate deduction shall not exceed Rs 30,000.

Sec 80D – Amount of deduction available to an individual (inclusive of preventive health check-up)			
Situation	Self, Spouse & Dependent Children Rs	Parent(s) whether or not dependent Rs	Total deduction u/s 80D Rs
All below the age of 60 years	25,000	25,000	50,000
Assessee and his family less than 60 years and parents above 60 years	25,000	30,000	55,000
Assessee and his family have attained the age of 60 years and above	30,000	30,000	60,000
Sec 80-D Amount of deduction available to a HUF (inclusive of preventive health check-up)			
One or more member of HUF is a senior citizen			30,000
None of the members is a senior citizen			25,000

Illustration 6

Raj and his wife are not senior citizens. Raj pays mediclaim insurance of Rs 18,000 for self, Rs 20,000 for his wife, and Rs 5,000 his two independent sons. He also pays Rs 18,000 for each of his parents who are senior citizens .Calculate the amount of deduction allowable u/s 80D.

Solution

Amount of deduction u/s 80D		
Premium in respect of wife		Rs 18,000
Premium for himself		Rs. 20,000
Premium in respect of children (not dependent)		Nil
Total Rs 38,000 restricted to		Rs 25,000
Add : Premium in respect of parents (senior citizens) Rs 36,000 restricted to maximum		Rs 30,000
Deduction available u/s 80D		Rs 55,000

4.5 Sec 80DD: Deduction in respect of expenses on maintenance and medical treatment of a dependent who is a person with disability.

(i) **Eligible assessee:** Individual and Hindu undivided family, who is a resident of India. Other assessees not eligible.

(ii) **Eligible Payments:**

a. Expenditure incurred for medical treatment including nursing, training and rehabilitation of a dependent, being a person with disability or

b. any amount paid or deposited under a scheme framed by the or any other insurer or the administrator or the specified company (UTI) approved by the Board in this behalf for the maintenance of a dependent, being a person with disability.

(iii) **Amount of Deduction :** Rs 75,000 in all cases , Rs.1,00,000, if dependent person suffers from severe disability

So long the assessee incurs some amount of eligible expenditure, the deduction will be allowed irrespective of the amount actually spent. It is not necessary to spend full amount of Rs 75,000 or One lakh rupees.

(iv) **Conditions for of Deduction :**

The following conditions should be satisfied to claim deduction:

(a) Deduction is available in respect of a "dependent" person.

(b) A dependent person means:-

- Spouse, children, parents, brothers or sisters of an individual or any of them.
- A member of a Hindu undivided family.

(c) Such person must be dependent wholly or mainly on such individual or Hindu undivided family for support and maintenance.

(d) Such dependent person must not claim deduction u/s 80U while computing his total income for that assessment year;

(e) The assessee nominates either the handicapped dependent or any other person or trust to receive the payment under the scheme for the benefit of the handicapped dependent;

(f) In the event of the death of the subscriber assessee, the amount of annuity or lump-sum under the scheme is paid for the benefit of the handicapped dependent.

(g) If the handicapped dependent predeceases the subscriber assessee, then the amount so received shall form part of the

total income of the subscriber assessee in the previous year in which the amount is received.

- (h) The assessee must furnish a certificate from a neurologist, a pediatric neurologist, in case of children,) or a civil surgeon or Chief Medical Officer of a Government hospital in form 10IA (in case of autism, cerebral palsy or multiple disability)
- (i) Where the condition of disability requires reassessment, a fresh certificate shall have to be obtained on expiry of the period mentioned in the original certificate.

4.6 Deduction in respect of medical Treatment-Sec. 80DDB

Eligible assessee: Individual and Hindu undivided family, who is a resident of India. Other assesseees not eligible

Eligible Payments:

Amount actually paid for medical treatment of specified disease or ailment of the assessee himself or a person dependent on him or a member of HUF

Amount of Deduction :

- Amount actually paid in the previous year or
- Rs. 40,000 or
- Rs 60,000, if such person or member is a senior citizen, or
- Rs 80,000, if the person or member is a very senior citizen.

Whichever is lower?

Other Points

(a) *"Dependent relative" means*

- a. *an individual himself ,*
- b. *spouse, children, parents or brothers and sisters of an individual , or*
- c. *a member of the HUF, who is wholly or mainly dependent for support and maintenance on the individual or the HUF*

(b) *"senior citizen" means an individual resident in India who is of the age of 60 years or more at any time during the relevant previous year;*

(c) *"very senior citizen" means an individual resident in India who is of the age of 80 years or more at any time during the relevant previous year,*

(d) The assessee shall furnish with the return of income, a certificate in prescribed form, from a neurologist, an oncologist, a urologist, a hematologist, an immunologist or such other prescribed specialist, working in a Government hospital;

(e) Amount of deduction shall be reduced by any amount received under an insurance from an insurer, or reimbursed by an employer

4.7 Deduction in respect of interest on loan taken for higher education Sec 80E

Eligible assessee:

Any individual assessee, (whether resident or non-resident) who has taken loan from a financial institution or any approved charitable institution for pursuing higher studies of himself or his relative

Amount and term of deduction:

- Interest on such loan paid by the assessee without any limit.
- Upto a maximum period of 8 years from the year in which the payment of interest on the loan begins or till the interest is paid in full, whichever is earlier.

Other Points

- 1) "Higher education" means any course or study pursued after passing Senior Secondary Education or its equivalent from any Government recognized school, Board or university.
- 2) "Course" may be any post-SSC course whether full -time or part time any Government recognised school, Board or university.
- 3) Higher education may be for the assessee himself or any of his relatives. Relative means the spouse and children of the assessee or the student for whom such individual is the guardian.
- 4) The deduction can be claimed by the student assessee himself if the interest is paid by him or his relative (say father), if interest on the student's loan is paid by the relative.

Illustration: 7

Advise A on the deduction in respect of interest on loan of Rs. 10 lakhs taken from SBI on 01/04/2014 for doing MBA repayable in 10 equal annual instalment carrying interest @ 10% per annum.

Solution:

A being the student himself, is eligible to get deduction/s 80E. A will be entitled to claim interest as under :-

Assessment Year	Interest allowable u/s 80E
2014-15	100,000
2015-16	90,000
2016-17	80,000
2017-18	70,000
2018-19	60,000
2019-20	50,000
2020-21	40,000
2021-22	30,000

Thereafter, for the remaining two years, no deduction will be available.

Illustration: 8

Will B father of A be entitled to deduction U/s 80E in respect of interest paid on A's Loan?

Solution:

Yes, if father pays the interest, he will be entitled to claim the deduction.

4.8 Deduction in case of a Person with Disability – 80U

Eligible assessee_:

- Individual resident of India
- with at least 40% disability
- at any time during the previous year.

Amount of deduction;

- Person with minimum disability of 40%- Rs 75,000 ;
- Persons with severe disability of over 80% - Rs. 1,25,000

Other Points

- 1) The deduction u/s 80U of Rs 75,000 / 1,25,000 is of a flat amount without any requirement for spending that amount.
- 2) Mere submission of a disability certificate in the prescribed form will be enough to avail the deduction along with the return of income of the assessment year for which the deduction is claimed for the first time.
- 3) Where the condition of disability requires reassessment of its extent after a period stipulated in the medical certificate, deduction for any year falling after the expiry of such period shall be allowed only if a new certificate is obtained and furnished.

4) "Disability" means blindness, low vision, leprosy-cured, hearing impairment, locomotor disability, mental retardation, mental illness, autism, cerebral palsy and multiple disabilities.

5) "Person with disability" & "Person with severe disability" have been defined in the Persons with Disabilities (Equal Opportunities, Protection of Rights & Full Participation) Act, or the National Trust for Welfare of Persons with Autism, Cerebral Palsy, Mental Retardation & Multiple Disabilities Act, 1995.

5. ILLUSTRATION

S presents the following data for the previous year 2017-18.

1. Business income Rs.8,10,000
2. Capital Gains Rs. 3,15,000
3. Payment of medical insurance premium on own life Rs.5,000
4. He pays Rs. 20,000 to GIC for maintenance of his severely disabled son under an approved scheme.
5. He has borrowed Rs 5,00,000 as educational loan for his younger son who pursues MBA from IIM and pays 10% interest on the loan.
6. S himself his severely disabled.

Determine the income of S for the assessment year 2018-19

Solution:

Computation of Total Income of X

		Rs
Business Income		8,10,000
Capital gains		3,15,000
Gross Total Income		11,25,000
Deductions under chapter -VIA-		
80D :Mediclaime	5,000	
80DD:Maintenance of dependent with severe disability	*1,00,000	
80E interest on study loan	50,000	
80U :Severe disability	*1,25,000	
Total Deductions under chapter -VIA		2,80,000
Total Income		8,45,000

For 80U full deduction available. Amt spent not relevant

6. SELF-EXAMINATION QUESTIONS:

1. Enumerate various incomes, exempt from under Section 10.
2. Explain the difference between deduction and exemption with 3 suitable examples.
3. Define Gross Total Income.
4. Explain the deduction u/s 80C of the Income Tax Act, 1961.
5. What is the amount of maximum deductions u/s 80D?
6. Briefly explain the provisions relating to deductions from the gross total income in the case of blind or physically handicapped person.
7. Enumerate exemptions available to foreign nationals in India.
8. Write short notes on:
 - a) Gratuity
 - b) Leave Salary
 - c) Retrenchment Compensation
 - d) House Rent Allowance
 - e) Dividends
 - f) Income of a minor child
9. Manan gets Rs 8,000 by letting out his agricultural land to a tenant who used the land for vermiculture. Clarify if Manan would be eligible for exemption for agricultural income with appropriate reasons.
10. The net profit as per the P & L A/c was Rs. 2,85,000 after taking credit of Rs. 45,000 received on maturity of LIC policy and Rs. 30,000 as Interest from government securities and donation of Rs. 40,000 to BMC for promotion of family planning and Rs 5,000 as alms to destitute. He also pays Mediclaim for Rs. 10,000 in cash and Rs. 10,000 by a credit card and Rs. Rs. 25,000 for his 70 year old father. Compute total income for the A.Y.2018-19.
11. A Resident person, who is physically handicapped (75%) earns a net income of Rs 5, 76,000 from a consultancy business run by him. Compute his total income for the AY 2018-19.

(Ans: Bus. Income 2,47,000, Other Sources 30,000 GTI 2,77,000, Tot. inc. 2,47,000)

(Ans : Business income 576,000, deductions, 80U- 75,000 total Income 5,01,000)



COMPUTATION OF TOTAL INCOME

Synopsis

1. Introduction and Objective
2. Typical Illustrations on computation of income
3. Filing of Returns
4. Advance Tax
5. Self Assessment Questions.

1. INTRODUCTION AND OBJECTIVES

The lesson deals with procedural aspect of law in respect of like filing of income tax returns and payment of advance tax and other incidental matters like procedure for computation of total income of individuals, firms and companies, computation of tax liability etc.

As per the syllabus , law applicable as on as on 01/04/2018 will be considered for computation of total income for the assessment year 2018-19 (previous year 2017—18). Further, the computation will be restricted to not more than two heads of income and two deductions at a time.

2. COMPUTATION OF TAXABLE INCOME-

2.1 Taxation of Individuals

Following are the salient features of the procedure relating to preparation of income tax returns for the financial year 2017-18 relevant to assessment year 2018-19.

Step -1 Collection of preliminary details :

- i. Name of the assessee
- ii. Birth date and age
- iii. Gender
- iv. Email address
- v. Mobile number
- vi. PAN
- vii. Aadhar No and linkage with PAN
- viii. GST No , if any
- ix. Residential status

- x. Assessment year-2018-19
- xi. Pervious year-2017-18
- xii. Detail of parents and age
- xiii. Detail of children and age
- xiv. List of Relatives and Associate concerns
- xv. List of investments in saving schemes like LIC, PF etc.
- xvi. Insurance premium paid
- xvii. Premium for insurance
- xviii. Details of handicapped dependents

These details are relevant to ascertain :-

- i. applicable tax rate e.g. woman, senior citizen, super senior citizen etc.;
 - ii. deductions e. g. insurance premium, handicapped assessee, education loan etc. ;
 - iii. disallowances based on relation as in 40A(2); and or
 - iv. exemption based on relation e.g. gifts from relatives u/s 56, 80U, 80D etc. .
2. Computation of income under the five heads of income as per the applicable provisions of law.
 3. Income of other assesseees; e.g. minor children, spouse etc., which are to be included as per the clubbing provisions given in sections 60-64.
 4. Aggregate of income from all such sources excluding the exempt income is called the Gross total Income.
 5. From the Gross Total Income reduce the amount of deductions available in Chapter VI A of the Act.
 6. The result will be the total income.
 7. Compute the tax liability at appropriate rate applicable including special rates applicable to some items of income –horse race , Capital gains on shares etc.
 8. From the tax liability, any tax rebates are to be reduced.
 9. The result will be the net tax liability, from which any amounts deducted at source (TDS) or Tax Collected at Source (TCS), and taxes paid in advance are reduced.
 10. The final balance, if any, is payable as self –assessment tax u/s 140A before filing the return of income. If the advance tax and

TDS are more than the tax payable, the excess is shown as the refund due.

11. Other Important Points

- a) Agricultural income in excess of Rs 5,000 is added to the total income and tax is computed on such total income. From the tax so computed, tax on agricultural income is separately computed by adding Rs 2,50,000 to the agricultural income. Difference of the two, will be the tax liability
- b) Interest and remuneration payable to partners will be taxable if they are allowed in the hands of firm. Profit from the firm exempt in the hands of the partners as it is taxable in the hands of the firm.
- c) Income of HUF is to be excluded as tax on such income will be payable by the HUF.
- d) Any loan taken from a closely held company is deemed dividend u/s 2(22)(e), if the hands of the individual if the individual and his relatives hold 10% voting power therein.

12. Income Tax Rates for Assessment Year 2018-19

A. In case of an Individual (resident or non-resident) or HUF or Association of Person or Body of Individual or any other artificial juridical person

Individuals	Senior Citizens	Very Senior Citizens	Tax Rate
0- 2,50,000	0- 3,00,000	0-5,00,000	NIL
250,001 5,00,000	3,00,001- 5,00,000	-NA	5%
5,00,001-10,00,000			20%
10,00,001 and above			30%
Surcharge on income tax if total income exceeds Rs 50 lakh but below Rs 1 crore.			10%
Surcharge if the total income exceeds Rs 1 crore			15%
Surcharge shall not exceed 70% of the amount of income tax payable on income over Rs 50 lakh /1 Cr.			
Rebate under 87A- Rs 2500 or 100% income tax (whichever is low) for the individuals having total income Rs 3,00,000 or less. (Effectively exemption limit for individual			

is Rs 3 lakh	
Education Cess (EC) on Tax amount	2%
Secondary and Higher Education Cess on tax and surcharge (SHEC) on tax amount	1%
<ol style="list-style-type: none"> 1. Senior Citizen is an individual, who has reached the age of 60 years at any time during the previous year but has not reached 80 years of the age as on the last day of the previous year. 2. Very Senior Citizen is an individual, who has reached the age of 80 years at any time during the previous year. 3. No basic exemption or allowance or expenditure shall be allowed to the assessee under any provision of the Income-tax Act, 1961 in computing deemed income., unexplained income, investments, money etc. chargeable under sections 68/69/69A/69B/69C/69D [Section 115BBE] Set-off of losses not permissible against such income. These provisions were brought in the wake of demonetization of high denomination currency notes. 	

PROCEDURE OF COMPUTATION:

A. Preliminary Information
Name and address of the assessee , PAN GST No E mail Residential Status Assessment Year 2018-19 Previous Year -2017-18
B. Computation of Total Income
<ol style="list-style-type: none"> 1. Income from Salary 2. Income from House Property 3. Profit and Gain of business and Profession 4. Capital Gains 5. Income from Other Sources
C. Gross Total Income (Total of B 1 to 5) (excluding exempt income)
D. Deduction under chapter VIA
E. Total Income [D-E]
F. Ascertain Tax Liability

Tax at applicable rates + Surcharge (after marginal relief)
Add –Education Cess -2 % on tax
Add Secondary and Higher Education Cess @ 1% of tax
G. Less : Rebates, Advance Tax , TDS , TCS
H. Add : Interest Payable to Government
I Self Assessment Tax / Refund Due (F-G+H)

Illustration -1.

Ascertain the tax liability of Rajesh, whose total income is Rs 5 lakh. A also show if there will be any difference in the tax liability if he also has agricultural income Rs 2 lakh.

Solution

I Tax on Income of Rs 5 lakh

	Rs
Tax on first Rs 2,50,000	NIL
On Next Rs 2,50,000 @ 5%	12,500
Total	12,500
Less Rebate U/s 87A	0
	12,500
Add Cess EC+ SHEC -3%	375
Total Tax on Rs 5,00,000	12,875

II If Income includes Agricultural income

(a) Tax on Total income plus agricultural income
Rs 5 lakh +2 lakh = Rs 7 lakh

	Rs
Tax on first Rs 2,50,000	NIL
On Next Rs 2,50,000 @ 5%	12,500
On Balance Rs 2,00,000 @ 20%	40,000
	52,500
Add Cess EC+SHEC	1,575
Total Tax on Rs 7,00,000	54,075

(b) Tax on basic limit plus agriculture income
-Rs. 2,00,000+2,50,000 = Rs 4,50,000

	Rs
Tax on first Rs 2,50,000	NIL
On Next Rs 2,00,000 @ 5%	10,000
	10,000
Add Cess EC+SHEC	300
Total Tax on Rs 4,50,00	10,300

(c) Tax payable (a)- (b) or Rs 54,075 – 10,300= Rs 43,775

From the above, tax liability works out to Rs 43,775 against the normal tax liability of Rs 12,875, implying that agricultural income is indirectly taxed.

2.3. Specific points applicable to Partnership Firms including Limited Liability Partnerships (LLP)

A. Tax Rates

- Tax Rate uniform 30 % without any exemption ;
- Plus surcharge @ 12% of tax ,if firm's income exceeds Rs 1 Cr (Subject to marginal relief), and
- EC+ SHEC @ 3% of tax plus surcharge

B. Classification of firms :

As per Section 184 the partnership firm are classified as

- (a) Partnership firm assessed as such (PFAS) ,and
- (b) Partnership firm assessed as an association of person.

C. Procedural requirements for firm :-

- i. A firm shall be evidenced by a partnership deed containing inter alia the individual shares of the partners. [Sec. 184(1)]
- ii. The firm must file -
 - a. a certified copy of the partnership deed along with the return of income in the first year. [Sec. 184 (2)]
 - b. a certified copy of the revised deed in the year , when there is a change in the constitution of the firm or in the sharing ratio of partners -[Sec. 184(4)]
- iii. The firm will continue to be assessed as firm after the first year, unless,
 - a. there is a change in firm's constitution or partners profit sharing ratio, and
 - b. the firm does not satisfy the above conditions. [Sec. 184(3)] ;and
 - c. The firms fails in compliance as specified in Sec. 144 [Sec. 184(5)]
- iv. A copy of the partnership deed shall be certified in writing by
 - a. all the major partners ; and
 - b. all the major partners in the firm immediately before the dissolution ,where return is filed after the firm's its

dissolution.; Legal heir can sign for a deceased a partner.
[Sec. 184(2) Expl.]

- v. In computing the income of the firm remuneration and interest payable shall be allowed only from the date of deed and to the extent specified the deed.
- D. A firm not assessable as a firm it will be treated as AOP and shall pay tax at the maximum marginal rate. The income will taxable in the hands of partners subject to rebate u/s 86.

2.4. Specific points applicable to Companies:

A. Rates of Tax applicable to companies

- I. **Tax Rates for Domestic Companies** whether (a) Widely held or (b) Closely held companies
 - 25% - Where gross receipt of the company does not exceed Rs. 50 crore.
 - 30% For other companies r

Surcharge:

- 7% of tax where total income exceeds Rs. 1 crore
- 12% of tax where total income exceeds Rs. 10 crore

Education cess and SHEC 3% on tax and surcharge

II. Tax Rates for Foreign Companies @ 40% ,

Surcharge

- 2% if the total income exceeds Rs 1 Crore , and
- 10% if *the total income exceeds Rs 10 Crore* , and

Education cess and SHEC 3% on tax and surcharge

B. Provision applicable on companies

There are several provision in the Act such as excessive payment to directors and their relatives u/s 40A(2), amortization of preliminary expenses u/s 35D , merger, demerger, amalgamation , ESOP/ESOS , certain deductions under chapter VIA , payment of Minimum alternative Tax 18.5%) u/s 155JA/JB etc., which are applicable only to company assesseees. These provisions, to the extent covered by the syllabus have been taken up at their appropriate place.

3. ILLUSTRATIONS

Illustration 1

Compute the taxable income of Mangesh for the AY 2018-19 from the following and also compute the tax liability:

Profit and Loss Account for the year ended 31st March, 2018			
Particulars	Rs.	Particulars	Rs.
To Salaries	2,10,000	By Gross Profit	10,18,000
To Rent	20,000	By Interest on Bank FD	8,000
To postage	7,000	By Dividend-Indian Co	20,000
To Stationery & Ptg	27,000	By dividend from - Co-Op Bank	2,000
To Advertising Exp.	20,000	By Lottery Prize	15,000
To Repairs to Office	22,700	By Interest on Debentures	5,000
To Conveyance	17,000		
To Income Tax	30,000		
To IT scrutiny Exp	4,000		
To CA's Fees for Tax	10,000		
To Misc. Expenses	25,000		
To Depreciation	5,000		
To Donation	20,000		
To Net Profit	6,50,300		
	<u>10,68,000</u>		<u>10,68,000</u>

Additional Information:

- (1) Salaries include bonus due to employees Rs. 30,000 which was not paid before the due date of filing of Income Tax return.
- (2) Rent is paid for the residential house of Mr. Mangesh.
- (3) Repairs to office include a one-time cash payment of Rs. 20,000 on 18/08/2017.
- (4) Miscellaneous expenses include purchase of shares of an Indian company for Rs. 20,000.
- (5) Donations include charity of Rs. 15,000 and Rs 5,000 given to GIC for maintenance of his handicapped brother.
- (6) Depreciation as per Income tax rules is Rs. 4,000.

Solution:

Computation of Total Income of Mangesh for A.Y. 2018-19		
Particulars	Rs	Rs
Income from Business		
Net Profit as per P/L Account		6,50,300
<u>Add: Disallowable Expenditure</u>		
Bonus due but not paid u/s 43B	30,000	
Rent (Personal	20,000	
Purchase of share (Misc Exp)	20,000	
Income Tax	30,000	
Donation (15,000+ 5,000)	20,000	
Depreciation	<u>5,000</u>	<u>1,25,000</u>
		7,75,300
<u>Less: Income Considered Separately</u>		
Interest on Bank FD	8,000	
Dividend from Indian Company	20,000	
Dividend from Co-operative Bank	2,000	
Winning from Lottery	15,000	
Interest on Debentures of Ltd Co	<u>5,000</u>	<u>50,000</u>
		7,25,300

Less: Depreciation as per rules		<u>4,000</u>
INCOME FROM BUSINESS		7,21,300
II <u>Income from Other Sources</u>		
Interest on Bank FD	8,000	
Dividend from Indian Company (Exempt)	0	
Dividend from Co-operative Bank	2,000	
Winning from Lottery	15,000	
Interest on Debentures of Ltd Co	<u>5,000</u>	
INCOME FROM OTHER SOURCES		30,000
GROSS TOTAL INCOME		7,51,300
Less: Deductions- under Ch. VI-A		
80-DD: Maint. of handicapped dependant		<u>50,000</u>
TOTAL INCOME		<u>7,21,300</u>
Tax Payable		56,760
Surcharge -3%		<u>1703</u>
Total Tax Payable		58,463

Note: To claim deduction u/s 80DD, it is not necessary that there must be actual expenses incurred on handicapped dependent.

Illustration 2

Compute the total income and ascertain the tax liability of Sam for the A.Y. 2018-19 from the following Profit and Loss Account:

<u>Profit and Loss Account for the year ended 31st March, 2018.</u>			
Particulars	Rs.	Particulars	Rs.
To Salaries	1,30,000	By Gross Profit	9,67,000
To Rent	30,000	By UTI Dividend	9,000
To Entertainment Exp	18,000	By LIC Mutual	5,000
To Printing & Stn	25,000	By Gift from Mother	5,000
To Advt Exp	50,000	By Winning- Puzzle	12,000
To Motor Car Exp	30,000	By Interest on NSC	3,000

To Drawings	60,000		
To Income Tax	16,000		
To Embezzlement -Employee	7,000		
To Staff Welfare Exp	70,000		
To Donation	30,000		
To Depreciation	35,000		
To Net Profit	<u>5,00,000</u>		
Total	<u>10,01,000</u>		<u>10,01,000</u>

Additional Information:

- (1) Depreciation as per Income tax rules is Rs. 38,000.
- (2) Staff Welfare expenses include Rs. 20,000 for his own treatment.
- (3) 50% of the rent is paid for his residential house
- (4) Printing includes Rs. 5,000 paid for printing marriage cards for his daughter's marriage

Solution:

Computation of Total Income of Sam for AY: 2016-19			
	Rs	Rs	Rs
I <u>Income from Business</u>			
Net Profit as per P/L Account		5,00,000	
Add: Disallowable Expenditure			
Own Medical Expenses	20,000		
Rent (Personal)	15,000		
Printing of Marriage Cards	5,000		
Income Tax	16,000		
Donation	30,000		
Depreciation	35,000		
Drawings	<u>60,000</u>	<u>1,81,000</u>	

Less: Income Considered Separately		6,81,000	
UTI Dividend	9,000		
Income from LIC Mutual Fund	5,000		
Gift from Mother	5,000		
Winning from Crossword Puzzle	12,000		
Interest on NSC	<u>3,000</u>	<u>34,000</u>	
Less: Depreciation as per rules		6,47,000	
<u>INCOME FROM BUSINESS</u>		<u>38,000</u>	6,09,000
<u>II Income from Other Sources</u>			
UTI Dividend (exempt)		Nil	
LIC Mutual Fund (exempt)		Nil	
Gift from Mother (exempt)		Nil	
Winning from Crossword Puzzle		12,000	
Interest on NSC		<u>3,000</u>	
<u>INCOME FROM OTHER SOURCES</u>		<u>15000</u>	<u>15,000</u>
GROSS TOTAL INCOME			6,24,000
<u>Less:</u> Deductions under Chapter VI-A			
80-C NSC Interest Re-invested		3,000	<u>3000</u>
TOTAL INCOME			6,21,000
Tax Payable on Income			36,700
Surcharge @3%			1,101
Total Tax			37,801

Illustration 3

Joshi is a Chartered Accountant, Following is his Receipt and Payments Account for the year ended 31st March, 2018.

Receipts	Rs.	Payments	Rs.
To Cash & Bank B/f	70,000	By Office Rent	6,000
To Fees from Clients (net)	6,60,000	By Ptg & Stn	5,000
To Hon. For Articles	40,000	By Gifts to Staff	11,000
To Dividend-Indian Co	5,000	By General Exp.	14,000
To Interest– Bank SB A/c	2,000	By Motor Car Exp	16,000
To Interest.-on PO SB A/c	3,000	By Telephone Exp	12,000
To Interest- Bank FD	8,000	By Income Tax	40,000
To Int. on Govt Securities	6,000	By Drawings	1,20,000
To Sale of Motor Car	1,00,000	By Car Insurance	12,000
		By conveyance	13,000
		By Tally Software	19,000
		By LIC Premium paid	64,000
		By Salaries to Staff	12,000
		By Computer (cost)	50,000
		By Cash & Bank C/f	5,00,000
TOTAL	8,94,000	TOTAL	8,94,000

Additional Information:

- (1) Computer was purchased on July 1, 2017 and depreciation is allowed @ 60% on the same.
- (2) Opening WDV of Block of Motor Cars consisting of 2 Motor Cars was Rs. 2,50,000 and depreciation is allowed @ 20% on the same.
- (3) Personal use of the Motor car is estimated to be 25%.
- (4) Fees from clients are after TDS of Rs. 2,000.
- (5) General expenses include a sum of Rs. 4,000 given to his daughter as birthday gift.
- (6) Drawings include a sum of Rs. 30,000 given premium for self and family of Rs. 20,000 and Rs. 10,000 for his father, who is a senior citizen/.

Compute the net taxable income of Joshi for the AY 2018-197.

Solution:

Computation of Total Income of S. V. Joshi –Asst. Year 2018-19		
Particulars	Rs	Rs
<u>Income from Profession</u>		
Fees from Clients	5,60,000	
Add: Tax Deducted at Sources	<u>2,000</u>	5,62,000
Less: Allowable Expenses		
Depreciation on Motor Car	22,500	
Motor Car Expenses @ 75%	12,000	
Office Rent	6,000	
Printing and Stationery	5,000	
General Expenses	10,000	
Motor Car Insurance @ 75%	9,000	
Telephone Expenses	12,000	
Conveyance Expenses	13,000	
Depreciation on Computer @ 60%	30,000	
Salaries to Staff	2,000	
Gifts to Staff	<u>11,000</u>	- 1,32,500
<u>INCOME FROM BUSINESS</u>		5,29,500
<u>II Income from Other Sources:</u>		
Receipts for Writing Articles	40,000	
Interest on Fixed Deposit	8,000	
Interest on Government Securities	6,000	
Interest on SB Account	2,000	
Interest on PO Savings Account (exempt)	Nil	
Dividend from Indian Companies (exempt)	<u>Nil</u>	
INCOME FROM OTHER SOURCES	<u>56,000</u>	56,000
GROSS TOTAL INCOME		<u>5,85,500</u>
Less: Deductions under Chapter VI-A		
80-C Life Insurance paid	64,000	
80-D Medical insurance Premia : Rs 30,000 for father + Rs. 25,000 for self=maximum	<u>55,000</u>	1,19,000
TOTAL INCOME		4,66,500
Tax Payable on Income		10825
Surcharge @ 3%		325
Total Tax		11,150

Illustration 4

Compute total income and tax liability on the income of X from the particulars given below:

Basic pay: Rs. 16,000 pm

Education allowance for one child: Rs. 300 pm

Bonus: Rs. 20,000

Salary in lieu of leave: Rs. 15,000

He contributed Rs. 18,400 to the recognized provident fund and an equal amount was contributed by his employer. He received Rs. 14,000 from bank as interest, dividend of Rs. 10,000 from a foreign company and winning from horse race of Rs. 42,500 (gross). He paid Rs. 500 professional tax.

Solution

COMPUTATION OF TOTAL INCOME – A.Y. 2018-19		
Basic Salary 16,000 X 12)		1,92,000
Education allowance	(300 X 12) 3,600	
Less: Exempt	(100 X 12) <u>1,200</u>	2,400
Bonus		20,000
Leave Encashment		15,000
		2,29,400
Less Profession Tax		500
Income from Salaries		2,28,900
Dividend from foreign company	10,000	
Winnings from Horse Race	42,500	
Bank Interest	14,000	
Income from Other Sources		66,500
Total Income		2,95,400
Tax Payable		2270
Rebate U/s 87A -100% of Tax		2240
Balance payable		0
Total Tax		NIL

Illustration-5

ABC is a partnership Firm carrying on a business, in which A, B, and C are partners sharing profits and losses equally. In respect of Assessment Year 2018-19 it furnishes the following particulars (*amounts in Rs.*):

- 1 Net loss as per P/L A/c after debiting remuneration/ Interest to partners Rs 2,50,000

- 2 Remuneration paid to partner – A Rs 90,000, B Rs 60,000 & C Rs 30,000
- 3 Interest paid to partners @ 20% per annum on their capital of Rs 1,00,000 each as of 01/04/2017

You are required to work out the income of the firm and the partners A, B and C assuming that partners have no other income.

Solution:

COMPUTATION OF TOTAL INCOME OF FIRM		
Net Profit as per Profit and Loss A/c (Loss)		[2,50,000]
Add: Remuneration to Partners	1,80,000	
Interest to partners - 20,000 X3	60,000	2,40,000
Profit before remuneration & Interest		[10,000]
Less: Less: Interest allowable only upto 12		36,000
Profit before remuneration		
Max. Remuneration upto profit		1,50,000
LOSS		[1,86,000]

TAXABLE INCOME IN THE HANDS OF PARTNERS

	A	B	C
Salary	75000	50000	25000
Interest	12000	12000	12000
Total Income	87000	62000	37000

- Salary allowed as deduction to firm Rs 1,50,000 taxed in the hands of partners in the ratio of the salary paid to them by firm 90:60:30
- Interest allowed to firm will also be taxed in the hand of the partners
- Total Income of Partners i.e. Salary and Interest taxable as Profits and Gains from Business or Profession:
- Excess of salary and interest, which was disallowed in the hands of the firm is not liable to be taxed in the hands of the partners.

4. PAYMENT OF ADVANCE TAX -SECTIONS 207-219

4.1 All assessees are required to pay advance tax on their current income from all sources , if tax liability for payment of tax is Rs.10,000 or more- (S 208) .

4.2. Amount and due Dates for payment of Advance Tax;

Advance tax is payable four instalments by the companies and in three instalments by other assessees as per the following table:

PAYMENT OF ADVANCE TAX	
Due date of Instalment	Tax Payable as % of total tax
15 June	Not Less than 15%
15 September	Not Less than 45% Less tax paid (30%)
15 December	Not Less than 75% Less tax paid (30%)
15 March	Not Less than 100% Less tax paid (25%)
Tax payable by assessee covered under section 44AD /44ADA for presumed taxation 100% of tax payable before 15 March	
Payment made by 31 st March considered Advance Tax	

4.3. Miscellaneous;

- The Assessing officer may, serve a notice upon the assessee to pay advance tax on the basis of the last regular assessment and if the assessee does not pay the advance tax he/it shall be deemed to be an assessee in default.
- For shortfall / non- payment assessee will be liable to pay interest U/s 234 B and 234 C.

Illustration 6:

Explain the liability for Advance Tax payment by Ramesh whose Income is estimated to be Rs 8,00,000 for F. Y. 2017-18 .

Solution:

Tax payable on current income of Rs 8,00,000 works out at Rs 74,675 , which will be payable as under:-

I - 15%	15 June ,2017	Rs 11,201
II-45%	15 September,2017	Rs 22,403
III-75%	15 December,2017	Rs 22,403
IV- 100%	15 March,2018	Rs 18,668

Illustration-7:

Explain the liability for Advance Tax payment by Ramesh Limited whose Income is estimated at Rs 8,00,000 during the financial year 2017-18)

Solution:

Ramesh Ltd is a company assessee liable to pay tax of Rs 2,47,200 on total income of Rs 8,00,000 , which is more than Rs.10,000. Hence Ramesh Ltd is liable to pay advance tax as under:

Instalment	Last Date for payment	Amount payable
I – 15%	15th June,2012	Rs 37,080
II- 45%	15th September,2012	Rs 74,160
III-75%	15th December,2012	Rs 74,160
IV-100%	15th March,2013	Rs 61,800

5. FILING OF RETURNS- SEC 139(1) AND 139(5)

5.1. LIABILITY FOR FILING RETURNS:

Section 139(1) casts the burden of filing return of income or loss on assessee. For some of the assessee it is mandatory to file on or before the due date a return of income or loss for the previous year in prescribed form, verified in prescribed manner and setting forth such other particulars as may be prescribed

For the following, assessee filing the return of income is mandatory:

1. Companies and Firms

2. Every Person (other than a company or a firm,) if his total income or the total income of any other person in respect of which he is assessable under the Act during the previous year exceeds the basic exemption limit.

(3) 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 exceeds the basic exemption limit is required to file a return of his income or income of such other person–

2. For companies and other assesseees having tax audit or having income of Rs 10 lakhs or more , filing of return in a digitally signed electronic form is mandatory.(Section 139D)

5.2. DUE DATE FOR FILING RETURN OF INCOME;

A return of income has to be filed on or before the due date of filing return. , ‘Due date’ means -

- (a) 30th September of the assessment year, the assessee being -
- (i) a company; or
 - (ii) 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
 - (iii) 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.

(b) 31st July of the assessment year, in the case of any assessee other than those covered in (a) above.

Illustrations : -

1. XYZ Limited shall file the return of income for the A.Y. 2018-19 on or before 30/09/2018
2. X having income of Rs 50,000, is not liable to file his return of income.
3. Z has a loss of Rs 2 lakh, and his accounts are not audited, due date in his case will be 31/07/2018

5.3 REVISED RETURN – SECTION 139(5)

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.

From the above, it is apparent that a belated return and it cannot be revised. In any case, a belated return can be filed under S 139(4) before the end of the assessment year i.e. 31/03/2019 in case of a belated return for AY 2018-19.

5.4 OTHER POINTS:

- A. CBDT is vested with the powers to prescribe forms of return
- B. A return must be properly verified and signed by an individual or partner of a firm or a director of company etc.
- C. Consequences of late filing of return ;
 - Liability for Interest @ 1% per month U/s 234A
 - Penalty of Rs 5,000 if return filed before 31st December and 1,0000 if filed thereafter. Return can not be filed after March 31,2019 U/s 271
 - **Certain exemptions cannot be claimed.** Including u/s 11- Charities, 10(38)- LTCG etc
 - Return cannot be revised
 - Loss is not allowed to be carried forward.
- D. Return will not be treated defective if Self –assessment tax not paid
- E. A return cannot be revised if filed in response to notice u/s 142.
- F. Belated return can not be filed beyond the end of the assessment year

6. Prescribed returns for the Asst Year 2018-19 are as follows

- ITR-1: For Individuals being a resident other than not ordinarily resident having Income from salaries, one House Property, other source (Interest etc.). and having total income upto Rs. 50 lakh.
- ITR-2: For Individuals and HUF not having income from profits and gains of business or profession.
- ITR-3: For Individuals and HUF having income from profits & gains business & profession.
- ITR-4 (SUGAM): For presumptive income from business & profession.
- ITR-5: For persons other than,- (i) individual, (ii) HUF, (iii) company and (iv) person filing Form ITR-7.

- ITR-6: For Companies other than Companies Claiming Exemption under section 11.
- ITR-7: For Companies including Companies required to furnish return under section 139(4A), or section 139(4B), or section 139(4C), or section 139(4D), or section 139(4E), or section 139(4F).

4. SELF ASSESSMENT QUESTIONS

1. Discuss the provisions for payment of advance tax. .
2. Explain advance tax liability of Ms. ABC if her income will be Rs 15,00,000 for the financial year 2017-18.
3. What are the due dates of payment of advance tax by different assessees?
4. Mr. Ram gives you the Profit and Loss Account for the year ended 31st March, 2018. You are required to compute the total income of Ram for AY 2018-19 assuming that Ram has paid LIC premium of Rs. 5,000.and interest of Rs 25,000 for educational loan of his son.

Profit and Loss Account for the year ended 31 st March 2018			
Particulars	Rs.	Particulars	Rs.
To Opening Stock	1,60,000	By Sales	18,50,000
To Purchases	14,05,000	By Closing Stock	1,08,500
To Salaries	1,84,350	By Winnings from Lottery	5,000
To Office Expenses	70,040	By Interest on fixed deposits with bank	15,000
To Office Rent	20,000	By Interest on RBI Bonds (exempt u/s 10)	16,000
To Staff Welfare	13,000	By bad debts recovered	20,000
To Advertisement	65,000	By dividend from Indian companies	9,000
Exp. To Donations	5,000		
To R.D.D.	10,000		
To Mediclaim (Cash)	21,000		
To insurance	10,000		
To Income Tax	8,000		
To Depreciation	20,000		
To Net Profit	32,110		
	20,23,500		20,23,500

Additional Information:

- a) Advertisement expenses include Rs. 11,000 for advertisement in a souvenir of a local political party and Rs. 20,000 for introducing a new product in the market.

- b) Donations are given for books to poor students
- c) On August 10, 2015 furniture of Rs. 20,000 was purchased on credit the payment for which was made on April 2, 2016. The same was not recorded in the books of accounts. The rate of depreciation on furniture is 15% per annum. On other fixed assets, depreciation was charged exactly as per I.T. Rules.
- d) Bad debts recovered were allowed during the A.Y 2015-16.
5. Sheela who is suffering from a permanent disability, received the following emoluments from SWY Ltd, her employer for last 10 years during the year ended March 31, 2018: You are required to compute her total income for the AY 2018-19.

Basic Salary (Net) April 1, 2017 to September 30, 2017	Rs. 10,000 p.m. (TDS Rs 600 P.M) , (Profession Tax Rs 1,250 P.M.)
October 1, 2017 to March 31, 2018	Rs. 12,000 p.m. (TDS Rs. 700 p.m.) (Profession Tax Rs 1,250 P.M.)
Dearness Allowance	40% of basic salary
Entertainment Allowance (Actually spent Rs. 300 p.m.)	Rs. 500 p.m.
Bonus for the year	Rs. 8,000
Conveyance Allowance (Actually spent Rs. 800 p.m.)	Rs. 1,000 p.m.

- Commission from employer is 1% of turnover of Rs. 10 lakhs;.
 - She needs a personal physical attendant whose salary of Rs. 2,000 p.m. was paid by the employer.
 - She paid Mediciam insurance of Rs. 12,000 for himself and Rs. 5,000 for his brother. Statutory Provident Fund @ 10% of basic salary was deducted from her salary.
6. Mrs. Sweetie aged 66 years took voluntary retirement on January 1, 2018 from a private bank after completing 26 years and 11 months of service. She furnishes you with the following information: Compute her net taxable income for the AY 2018-19. After retirement, she delivers lectures as guest faculty in Indian Institute of Banking for which she receives honorarium of Rs. 22,000. She paid Mediciam premium of Rs. 13,200 by crossed cheque. She invests Rs. 50,000 in National Saving Certificates. She received gifts from her colleagues for Rs. 3,00,000 in January 2018 .

Basic Salary	Rs. 2,800 p.m.
Dearness Allowance	128% of basic salary
Conveyance Allowance (actual expenses. For official purpose Rs. 600 p.m.)	Rs. 900 p.m.
Gratuity	Rs. 1,29,200
Commuted pension	Rs. 67,500
Leave Encashment	3 months basic salary
Uncommuted pension	Rs. 2,500 p.m.
Voluntary retirement compensation	Rs. 8,72,000
Profession tax paid	Rs. 1,200

7. Compute total income of Krishna for the AY 2018-19 from the Profit and Loss Account of his proprietary concern for the year ended March 31, 2018

Particulars	Rs.	Particulars	Rs.
To Opening Stock	2,34,000	By Sales	12,40,000
To Purchase	10,00,000	By Closing Stock	2,05,000
To Office Salaries	57,000	By Income Tax Refund (including interest Rs. 2,000)	15,000
To Proprietor's Salaries	30,000	By Dividend from UTI	20,000
To Bad Debts	10,500	By Dividend from Y Ltd (an Indian Company)	25,000
To Advertisement	4,500	By Interest on PPF	5,000
To Fire Insurance Premium	6,000	By Lottery prize received	10,000
To Conveyance Exp	25,000		
To Interest on Proprietor's Funds	20,000		
To Medical Expenses	35,000		
To General Expenses	5,000		
To Wealth Tax paid	14,000		
To Residential Telephone expenses	30,000		
To Depreciation	20,000		
To Net Profit			1520,000
	15,20,000		

Additional Information

- The residential telephone is used half the time for office work.
- Purchases include Rs. 1,00,000 paid for cash purchases, exceeding the limits prescribed under Section 40A(3).
- General expenses include advance income tax of Rs. 10,000 paid during the year and Rs. 500 for purchase of lottery tickets.

- d) Depreciation allowable as per Income Tax Rules Rs. 25,000
 e) Agricultural income Rs.70,000.

8. Compute total income of R with 40% disability, from following information regarding his house property for the AY 2018-19

Particulars	HOUSE I	HOUSE II
Fair Rent	40,000	60,000
Municipal Valuation	55,000	50,000
Rent received	60,000	--
Municipal tax:		
(a) Paid by the tenant	4,000	--
(b) Paid by Ri	6,000	5,000
Interest on capital borrowed (due but not paid) for the purpose of construction of house property	6,000	13,000
Ground Rent	2,000	--
Insurance premium paid	1,500	--
Other information:		
(i) Interest from debentures in Y Ltd	12,000	--
(ii) Dividend from UTI	5,000	--
(iii) Bank interest from SBI	3,500	--
(iv) Winning from lottery	28,000	--
(v) Interest from Post Office Savings Account	5,000	--
(vi) Dividend from a co-operative society	5,000	



SECTION- II: INDIRECT TAXES

GOODS AND SERVICE TAX

1

GST – AN OVERVIEW

Synopsis

1. Introduction and Objective
2. Direct vs Indirect Taxes
3. Pre-GST Indirect Tax Structure
4. Historical Background of GST in India
5. Indian GST vis-à-vis GST in Other Countries
6. Concept of GST
7. Need for GST in India
8. Indirect taxes Subsumed in GST
9. Framework of GST in India
10. Benefits of GST
11. GST council
12. Goods and services tax network (GSTN)
13. Self-Examination Questions

1. INTRODUCTION AND OBJECTIVE

The lesson explains the concept and basic feature of direct and indirect taxes, the differences between the two types of taxes and principal direct and indirect taxes levied in India. The lesson further explains the concept, need and objective of Goods and Service Tax (GST) in India, its framework, the roadmap for its implementation, benefits accruing from implementation of GST and other incidental matters.

2. DIRECT VS INDIRECT TAXES

2.1. Tax

‘Tax’ is the money, people pay to the government. It is a forced payment; not something that people pay voluntarily. Tax is considered as the price of civilization to enable a government to

mobilise funds for governance, defence and development of the nation, provision of health, education, sanitary and other public welfare services, maintaining law and order and creation of infrastructure. In the modern times, taxation has become a powerful tool or a catalyst for implementing socio-economic goals of the governments and stimulating economic growth.

2.2. Types of taxes

2.2.1. Broadly, the taxes are of two types, viz. direct and indirect taxes.

2.2.2. Direct Tax

A direct tax is a personal tax directly paid to the government by a taxpayer, on whom it is imposed. A taxpayer cannot shift his burden on a third party. Income tax, wealth tax, estate duty and gift tax are some examples of direct taxes. Of late, wealth tax and estate duty have been abolished and gift tax has been partially merged with income tax.

2.2.3. Indirect Tax

An indirect tax is a tax paid by one person but borne by another person. Effectively, the taxpayer viz. the manufacturer, the trade of the goods or the service provider acts only as an agent or an intermediary between the government and the consumer. Indirect tax is a destination-based tax on consumption of goods and services. In the first instance, the taxpayer pays the tax to the government and recovers it from the end-consumer of the products or services by adding the amount of tax in their price. Thus, the tax burden is ultimately shifted on and borne by the end user or consumer of the goods or services.

Excise duty, customs duty, service tax, central sales tax (CST), value added tax (VAT), entry tax, purchase tax, entertainment tax, tax on lottery, betting and gambling, luxury tax, tax on advertisements are some examples of the indirect taxes. From 1 July 2017, barring some exceptions such as property tax; stamp duty, customs duty etc., most of the indirect taxes have been merged into one single uniform tax called Goods and Service Tax (GST).

2.2.4. Direct V/s indirect Taxes

2.2.4.1. Progressive and Regressive Taxes

Direct taxes are collected from the actual taxpayer according to his capacity to pay taxes. A person with higher income pays more taxes than a person with lower income. Therefore, direct taxes are considered progressive taxes.

In contrast, indirect taxes are uniformly collected from all consumers of goods and services regardless of their capacity to pay. Hence, the indirect taxes are reconsidered regressive taxes.

2.2.4.2. Larger Tax Base

Unlike the direct taxes, **indirect taxes** are uniformly spread over all sections of the population based on the value of goods and services consumed by them. Hence, they do not directly affect the actual taxpayers. Therefore, the indirect taxes create a larger tax base and provide a major source of revenue to the governments.

2.2.4.3. Inflationary Impact

Indirect taxes have an inflationary impact because the suppliers add the amount of tax paid in the prices of goods and services consumed.

2.2.4.4. Socio-economic Goals

Indirect taxes act as a catalyst or tool for achieving their socio-economic goals of the government. For instance, most governments impose steep taxes on luxury goods and services, “sin goods” or harmful goods such as tobacco, alcohol serving the twin goals of augmentation of revenue coupled with control on the consumption of such goods and services.

3. PRE-GST INDIRECT TAX STRUCTURE

3.1. Seventh schedule to the Constitution of India divides the legislative powers into three lists viz.

- List I-the Union List,
- List –II- the State List ; and
- List III the Concurrent List.

As per the Union List, direct taxes viz. Income Tax, Capital Gains and Corporate tax are in the domain of the Centre while right to levy Agricultural Income tax is vested in the states as per the State List.

3.2. For indirect taxes, the constitution provides two-tiered tax structure with the following features:-

- i. Under the Union list, Centre was authorised to levy following taxes, viz. :-
 - a. excise or tax on manufacture of goods except alcoholic liquor for human consumption, opium, narcotics etc.
 - b. tax on the value of all taxable services provided or to be provided.

- ii. The state list authorised the states to levy taxes on intra-state sale or consumption of goods. The taxes included VAT Excise on liquor, Luxury Tax etc.
- iii. Under the concurrent list, both the Centre and the states could levy taxes concurrently on some items. However, residual powers remained with the Centre.
- iv. Inter -state sales attracted both the excise duty and central sales tax.
- v. Central sales tax was levied by the centre but it was collected and retained entirely by the originating States.

3.3. These taxes were not mutually exclusive. When the goods were again sold in the course of intra-state sale, they attracted VAT on the gross value of the goods, which included the basic value, the excise duty charged by manufacturer and the profit by dealer. There was no set off or rebate in respect of one tax against the credit of another tax and *vice versa for the following reasons :-*

- a) Excise and service tax were central taxes on manufacture of goods or the component of service provided or to be provided.
- b) VAT was a state tax on sale of goods
- c) A seller of goods could not get set off excise on manufacture of goods and service tax on the service component of those goods paid to the Centre against the liability to pay VAT to the state.
- d) Conversely, a manufacturer or a service provider could not avail credit for VAT on purchase of inputs paid to the state against the tax liability for central taxes.

3.4. A service provider or a manufacturer could avail credit for the service tax or the excise duty paid on the inputs for providing taxable service or for manufacturing excisable goods, integrated at the central level both being the central taxes. No such credit was, however allowed for VAT paid on the inputs to the state government

3.5. Pre-GST sales tax regime was a combination of -

- a. An origin -based central sales tax levied in the state, from where the goods originated, and
- b. Destination based multipoint value added tax levied in the state- where the goods were consumed.

3.6. Hence, the country had a multi-tier indirect tax regime comprising of overlapping taxes levied by different authorities at different levels of the tax pyramid that denied credit or set off for the

taxes paid at the previous stages. Credit for the VAT paid on the inputs was denied to the manufacturer and the service provider and credit for the excise duty or the service tax paid was denied to the seller only because the excise duty and the service tax were the central taxes, but the VAT was a state tax. This resulted into complex cobweb of rules and regulations in different parts of the country having cascading tax effect.

3.7. The flaws in the indirect tax structure created the need for a uniform, integrated central tax with lower tax rates; efficient implementation and free credit across the board for various taxes paid and reduce the cascading effect of multiple taxes.

4. HISTORICAL BACKGROUND OF GST IN INDIA

4.1. In 2004, Kelkar Task Force recommended the idea of a fully integrated Goods and Services Tax (GST) on national basis. Accepting the recommendation of the Task force, the Government in the Union Budget 2007-08 fixed 1 April 2010 as the date for implementation of GST in India. No significant progress was made thereafter due to lack of consensus among the stakeholder states until 19 December 2014, when the Constitution (122nd Amendment) Bill, 2014 on GST was tabled in the parliament.

4.2. The bill was passed by Lok Sabha on 6 May 2015 and Rajya Sabha on 3 August 2016. After ratification by more than half of the stakeholder states, the bill received the presidential assent on 8 September 2016 and became The Constitution (101st Amendment) Act, 2016 clearing the decks for introduction of GST in India.

4.3. After several post amendment meetings among the states and the Centre, four Central GST legislations, the Central Goods and Services Tax (CGST) Bill, 2017, Integrated Goods and Services Tax (IGST) Bill, 2017, Union Territory Goods and Services Tax (UTGST) Bill, 2017 and Goods and Services Tax (Compensation to States) Bill, 2017 were introduced in the parliament on 27 March 2017 and promptly passed on 29 March 2017. The bills received the President's assent on 12 April 2017 resulting into enactment of the respective four Acts.

4.4. The States led by Telangana, Rajasthan, Chhattisgarh, Punjab, Goa and Bihar passed their respective State GST laws. Finally, at a special session of the parliament, at the stroke of midnight on 1 July 2017, India rolled out GST as its path breaking indirect tax reform on the principle of one nation -one tax.

5. INDIAN GST VIS-À-VIS GST IN OTHER COUNTRIES

5.1. Indian GST is a unified tax model for the entire country. It subsumes multiple indirect taxes such as excise duty, service tax, VAT, CST, luxury tax, entertainment tax, entry tax, etc. under the common umbrella of GST. The GST regime professes to create a pan-Indian common national market, facilitate Indian businesses to become globally competitive by creating an efficient, corruption-free and transparent tax regime with minimum bureaucratic red-tape facilitating the ease of business and making inter-state movement of goods easier.

5.2. India is one of the 160 countries across the world to implement unified tax model like GST. For record, France was the first country to implement GST in 1954 more than six decades ago. The United States does not have a unified tax model as the states have their own taxes.

5.3. Most countries have adopted a uniform GST subsuming all indirect taxes, grouped under one umbrella with the exception of Brazil and Canada, which opted for a dual-GST model. India followed the dual model having inbuilt concepts of UGST, SGST, CGST and IGST separately for central, state and Union territories and for inter-state sales.

5.4. Efficient implementation of a simple lower tax rate to yield higher revenue is the underlying principle of an efficient GST regime globally. Singapore and Malaysia have moderate GST rates at 8% and 6% respectively.

Canada has a dual system of GST with Harmonized Sales Tax (HSN) with tax rates of 0%, 5% and 15%, while GST in UK is at 20% with provision for lower rate, zero rate and exemptions.

Indian GST with a four-tier GST tax structure of 5%, 12%, 18% and 28%, , zero rate and exempted supply coupled with different state and central levy- i.e. CGST, SGST, UTGST, and IGST is one of the most complex and intricate tax regime in the world.

5.5. Different countries have different exemptions and threshold limits for liability for GST. The threshold limit of Rs 20 lakh to attract GST liability in India is among the lowest in the world. However, Indian GST provides for option of composition without claiming input tax credit restriction on issue of taxable invoices etc., which is likely to deter many from availing such schemes.

5.5. A stringent inflation control is necessary for an effective GST regime to protect consumers against price rise and profiteering. India, like Singapore and many other countries has initiated anti-profiteering laws at the retail level to protect consumers from price swindling.

5.6. Alcohol and petroleum products constitute about 40% of a states' revenue. Hence, most states did not concede their right to levy tax on these products. As a result, unlike other countries, alcohol and petroleum products are outside the purview of GST in India, with each state free to set its own rates. Input credit will not be available for the manufacturers using alcohol and petroleum products thus increasing the costs for the end consumer.

6. CONCEPT OF GST

6.1. GST is a tax levied **only** on the value added at each stage of supply chain comprising of manufacture, sale and consumption of taxable goods or services. The GST provides for a comprehensive and continuous chain of tax credits beginning from the manufacture or production of goods or provision of service up to the retailer or consumer to ensure that

(a) there is no cascading effect by levying tax on tax at each stage; and

(b) the tax is levied only on the value added at each stage of supply.

6.2. At each stage of supply, a supplier can avail input credit for the tax paid on the purchase of goods or services and set off this credit against the GST payable on the supply of goods and services be made by him to the next stage.

GST makes no difference between goods and services and both are treated at par and taxed at a single rate.

6.3. It is only the final consumer, who bears the GST charged by the last supplier in the supply chain, with set-off benefits at all the previous stages.

Illustration

(a) Assumed that goods is priced at Rs 25,000 by A and Rs. 28,000 by B with value addition is 20% . Rate of tax is assumed to be 6% each CGST/ STGST. Tax position will be as follows ;

Particulars	A to B	B to C	Tax Payable By B
Price charged for supply of goods/ services	25000	28,000	
CGST @ 6%	1500	1680	180
SGST @ 6%	1500	1680	180
Total price charged	28,000	31360	

Notes

1. A pays Rs ,3000 (1500 each CGST & STGST)
2. B's gross liability is Rs 3,360 (1680 each CGST & STGST)
3. B pays only Rs 360 (Rs 180 each CGST & STGST)
4. B gets input credit for tax paid to A 1500 each CGST & STGST
5. Government gets Full tax of Rs 3180 – 1500 from A and 180 from B
6. But for the ITC , the liability would be Ts 3,360 due to cascading effect of tax)

(b) A and B belong to different states, then A will charge IGST of Rs 3000 (12%) and B will get ITC of RS 3000 against IGST and pay the balance just as before. This is an example of seamless credit flow.

7. NEED FOR GST IN INDIA

The main flaw of the pre-GST tax regime was the existence of multiple taxes at both the central and state level without having an across the board credit system for taxes paid earlier. This imposed hindrance in smooth movements of goods across the country besides creating scope for arbitrage of rates at different places, interstate smuggling and grey markets for goods and services. India needed a uniform tax regime with lower rates and stringent implementation. Some other reasons are as under:-

- a. Integration of different taxes such as excise, VAT, luxury tax, entertainment tax, Octroi and CST so as to avoid multiple taxation of a transaction as both goods and services
- b. Replacement of multiple tax levies by a uniform tax regime in respect of goods and services both.
- c. Abatement of the cascading tax burden of tax on tax at different levels.
- d. Introduction of an indirect, comprehensive, broad based consumption Tax for any product or service throughout India
- e. Provision for a continuous chain of credits from the original producer or service provider to the retailer or end consumer for

taxes paid at earlier stages i.e. input credit to ensure the removal of cascading effect of multiple taxes.

- f. Imposition of tax only on the value added at every stage in the supply chain instead of tax on origin or manufacture of goods.
- g. Setting up an efficient tax regime free of corruption and bureaucratic red-tape to enable simplified tax compliance.
- h. Creation of a national market for goods and services.
- i. Safeguarding the interests of the states by opting for a dual-model GST with inbuilt provisions for CGST, SGST, UGST and IGST.

8. INDIRECT TAXES SUBSUMED IN INDIA

8.1. The principle objective of the GST is to reduce the complexities, remove the effect of cascading tax burden by introducing a new broad based tax regime which subsumes all the taxes levied on the sale of goods or provision of services by both the centre and the states and provide a larger pull for set off of taxes.

8.2. Principles of subsuming taxes

Following principles were applied to identify the indirect taxes levied on supply of goods or services to be subsumed, viz :-

- a. Only indirect taxes on goods and services were to be subsumed in GST.
- b. Such taxes were part of the supply chain i.e. manufacturer , service provider or retailer or consumer;
- c. The taxes resulted in free flow of tax credits in intra and inter-State levels;
- d. The taxes which were not specifically unrelated to supply of goods or services, e.g. stamp duty, municipal taxes etc. were not subsumed in GST. and
- e. The subsuming of the taxes maintained revenue neutrality and fairness between the central and the states.

8.3. Taxes subsumed or absorbed in GST

Based on the above principles, following taxes have been subsumed in GST.

Taxes subsumed or absorbed in GST	
Central Taxes	State Taxes
Central Excise Duty (CENVAT)	
Additional Excise Duties	VAT / Sales tax
Excise Duty under the Medicinal and Toiletries Preparations (Excise Duties) Act 1955	Entertainment tax except levied by the local bodies)

Service Tax	Luxury tax
Additional Customs Duty, commonly known as Countervailing Duty (CVD)	Taxes on lottery, betting and gambling
Special Additional Duty of Customs – 4% (SAD)	State Cesses and Surcharges wherever they relate to supply of goods and services
Surcharges and Cesses levied by Centre wherever they are in the nature of taxes on goods or services e.g. cess on rubber, tea, coffee, national calamity contingent duty etc.	Octroi and Entry Tax
Central Sales Tax phased out	Purchase Tax

8.4. Taxes not subsumed

Following taxes were not subsumed in GST:

- 1) Basic Customs Duty levied on Import of goods into India.
- 2) Exports Duty imposed on export of goods are not available in India in abundance,
- 3) Road and Passenger Tax ,
- 4) Toll Tax
- 5) Property Tax
- 6) Stamp Duty
- 7) Electricity Duty

8.4. Treatment of Specific goods

a) The Alcoholic Liquor for Human Consumption

Under Article 366, clause 12A, the supply of the alcoholic liquor for human consumption is outside the ambit of GST. The States will continue to impose tax on it. Moreover, CST on inter-state sales of alcohol products would also continue.

b) Tobacco Products

Tobacco and tobacco products being “Sin’ goods will be subjected to GST subject to a separate excise duty by the Centre.

c) Petroleum, Crude, High Speed Diesel (HSD) , Motor Spirit, Natural Gas and Aviation Turbine Fuel(ATF)

The states will continue to levy VAT on intra-state sales of petroleum products. Inter-state sales would continue to attract Central Sales Tax (CST). However, these products may be transitioned into the GST regime on a future date to be notified by the GST Council. Moreover, these products are also subject to levy of excise duty imposed by the Centre in addition to the VAT or GST.

d) Newspapers and newspaper advertisements

While there is no GST on newspaper, GST, advertisements are subject to levy of GST.

9. FRAMEWORK OF GST IN INDIA

9.1. GST is a destination-based tax applicable on all transactions involving supply of goods and services for a consideration subject to exceptions thereof. It extends to whole of India including the State of Jammu and Kashmir.

9.2. India has followed the dual GST model like Canada and Brazil. Under this model, both the Centre and the states may concurrently levy GST on intra-State taxable supply of goods or services or both.

9.3. The dual model of GST adopted in India comprises of the following components:-

- a) Central Goods and Service Tax (CGST) levied and collected by the Centre,
- b) State Goods and Service Tax (SGST) levied and collected by the states, or
 Union Territory Goods and Service Tax (UTGST) levied and collected by the Union Territories with legislatures or
 UTGST levied and collected by Union Territories without State Legislatures,

9.4. The Centre is empowered to levy Integrated Goods and Service Tax (IGST) on all the inter-state supply of taxable goods or service or both. IGST is almost equal to the sum total of CGST and SGST/UTGST.

9.5. Legislative Framework

Legislative formwork for levy and collection of GST is as under:

Type of GST	Legislation	Levied and collected by
CGST	CGST Act, 2017	Central Government
UTGST	UTGST Act, 2017	Union territories without State legislatures viz. Andaman and Nicobar Islands, Lakshadweep, Dadra and Nagar Haveli, Daman and Diu and Chandigarh
SGST	SGST Acts	Respective States and union territories with their own legislatures viz. Delhi and Puducherry

Different state laws providing for levy of SGST and CGST Act are by and large uniform in respect of the basic features of the tax, chargeability, taxable event, taxable person, classification and

valuation of goods and services, procedure for collection and levy of tax etc. to keep the concept to of dual GST in harmony.

10. BENEFITS OF GST

GST will be beneficial for the economic growth of the country and all the stakeholders in the following ways: -

1. Common National Market

GST has removed economic barriers and created an integrated economy with a unified common national market with harmonised laws, common tax rates and procedures.

2. Single Tax

GST subsumes most of the central and state taxes into a single tax and provides for a seamless credit scheme in the supply chain. Elimination of multiple taxes and double taxation will remove the effect of cascading.

3. Competitive prices

As a result of mitigation of ill effects of cascading, average tax burden is likely to come down, which is expected to bring down the prices of goods and services and make them market friendly and competitive.

4. Make in India

- a) GST will give a major boost to the 'Make in India' initiative of the Government of India by making goods and services produced in India competitive in the national as well as international market giving rise to the exports and also demand for goods and services in domestic markets.
- b) More consumption and higher exports will result in higher production and manufacturing activities leading the growth of the industries to turn India into a "Manufacturing hub".
- c) Increased manufacturing will create additional job opportunities in industry and service sectors.

5. Foreign Investment

Unified common national market will attract Foreign Direct investment necessary for the "Make in India" campaign.

6. Ease of Doing Business

- a) Mitigation of double taxation will make doing business easier and also reduce litigation and disputes relating to double taxation of a transaction as both goods and services.
- b) GST is a simple tax regime with fewer exemptions.

- c) It will reduce multiple taxes leading to simplification and uniformity and the need for multiple record keeping for a variety of taxes saving cost of compliance.
- d) GST envisages simplified and automated procedures for various processes such as registration, returns, refunds, tax payments, etc.
- e) GST prescribes common procedures for registration, refund, filing of returns, classification of goods, etc. will make the taxation system more certain.
- f) Public interface between the taxpayer and the tax administration will be considerably reduced as interaction will be through the common GSTN portal.
- g) GST regime will improve environment of compliance with online filing of returns, verification of input credits and encourage more paper trail of transactions.
- h) Electronic matching of input tax credits all-across India thus making the process more transparent and accountable
- i) Timelines are prescribed for obtaining registration, refunds, etc.
- j) GST will help in improving liquidity of the business.

7. Economic growth and Tax compliance

- a) GST will widen the tax base, improve compliance by the taxpayers, and increase the tax revenues of the government.
- b) A cumulative effect of high production, export etc. Will improve the overall investment climate in the country and be helpful in growth in economic activities, increase the GDP, boost economic growth and remove poverty.
- c) Uniform GST rates across the country will reduce tax avoidance or evasion by eliminating rate arbitrage between different stage or intra and inter-State sales

8. Consumers

- a) Final price of goods is expected to be lower due to seamless flow of input tax credit between the manufacturer, retailer and service supplier.
- b) A large number of small retailers with turnover up to Rs 20 lakhs are exempted from tax and those having turnover up to Rs 1.5 Crore will be covered under a composition scheme with low to moderate tax rates. This will mean purchases from such retailers at relatively lower prices giving quantum increase to consumption of goods.

9. Uniformity in tax rates , nomenclature and interpretation :

GST will ensure uniformity in rates of tax and interpretation.

While, “goods include all materials, commodities, and articles”, service would include anything done for consideration which is not goods. This will encompass all goods and services in its scope. Further the classification of goods and services is done as per HSN or Harmonised System of Nomenclature). A new scheme for classification of Services has been devised under various sections, headings and groups.

11. GST COUNCIL

11.1. Under the newly inserted Article 279A, the President of India is vested with the power to constitute a joint forum of the Centre and States Goods & Services Tax Council (GST Council). These provisions came into force on 12th September 2016. Soon thereafter, the President constituted the GST Council on 15th September 2016.

11.2. The composition of the GST Council is as under;

- i. Chairperson - Union Finance Minister
- ii. Vice Chairperson – Chosen from amongst the Finance Ministers of the State Governments
- iii. Ex-Officio Secretary -The Secretary (Revenue) (as per the decision of the Union cabinet on 12 September 2016.
- iv. Members
 - a. Union Minister of State (Finance)/Revenue
 - b. All Ministers of Finance / Taxation of each State or any other Minister nominated by the States or Union Territories with legislatures
- v. Permanent invitee (non-voting) -Chairperson, Central Board of Excise and Customs (CBEC)
- vi. **GST Council Secretariat**

The GST Council is managed by the GST Council Secretariat) comprising of the officers taken on deputation from both the States and the Centre. Funds for running the Secretariat will be made available and borne by the Centre. The government has appointed one Additional Secretary and four Commissioners to the Secretariat.

11.3 The functions of the Council

The GST Council shall perform the following functions, viz. :-

- a. To make recommendations to the Union and the States on everything related to GST including laws, rules and tax rates, exemptions, threshold limits, dispute resolution etc.

- b. To recommend the date on which GST be levied on petroleum crude, high speed diesel, motor spirit, natural gas and aviation turbine fuel.

11.4. Decision making at the Council

- a. Every decision of the council shall be taken in a meeting.
- b. Quorum for every such meeting shall be not less than 50% of total members.
- c. Every decision of the GST Council is taken by a majority of not less than three-fourth (75%) of the weighted votes of the members present and voting.
- d. Vote of the Centre has a weight age of one-third of total votes cast.
- e. Votes of all the State Governments taken together has a weight age of two-thirds of the total votes cast, in that meeting.

Example:

At a meeting of the Council, 24 members are present, of which 23 members are from the states and one represents the Centre. The weight age of votes will work as under :

- Total votes cast 24
- Weight age of Centre - $\frac{1}{3}$ of 24 = 8 votes
- Weight age of the 23 members of the States taken together - 16 votes i.e. or 0.6956 votes each member.

To pass a resolution by votes required $\frac{3}{4}$ of 24 = 18 votes, the Central Government will have weightage of 8

It will need support of 10 states to take the decision.

Interestingly, all the states present in above case concur, then only the decision can be taken if the Centre does not agree. No decision can be taken when states are not unanimous without the support of the Central Government as the requisite majority of 75%.

11.5. Decision not to be invalid

Any defect in procedures adopted, or appointment of members or in constitution of the council or non- filling up of any vacancy shall not render the decision making by the Council invalid.

- 11.6.** The GST Council has held as many as 28 meetings by end of July 2018 and has taken several decisions such as simplification of procedures, composition, e-way bills, threshold limit for registration, periodicity of returns to be filed,

IGST credit and measures for removal of difficulties including revision of GST rates.

12. GOODS AND SERVICES TAX NETWORK (GSTN)

12.1. GST regime primarily relies upon technology-based compliances. Hence, a Company Goods and Service Network (GSTN) was incorporated as a special purpose vehicle as a non – profit organisation under the provisions of section 8 of the Companies Act, 2013 with the initial capital of Rs. 10 Crore. The Government of India holds 24.5% equity in GSTN and all States including Delhi and Puducherry, and the Empowered Committee of State Finance Ministers (EC), together hold another 24.5%. Balance 51% equity is with non-Government financial institutions.

12.2. The company set up a single portal www.gst.gov.in to provide IT infrastructure and all GST related services to the Central and State Governments, taxpayers and other stakeholders for implementation of the Goods and Services Tax (GST).

12.3. The portal also aims to establish a uniform interface linkage for the taxpayer and a common and shared IT infrastructure between the Centre, Union Territories and, States. The portal is accessible over Internet by taxpayers and tax professionals like Chartered Accountants, Tax Advocates Banks, accounting and tax authorities and other stakeholders and Intranet by Tax Officials etc.

12.4. The functions of the GSTN

Primarily, GSTN provides three front end services to the taxpayers namely registration, payment and return through GST Common Portal. Its main functions are as under:-

- a) To facilitate Registration of the taxpayer with the help of IT, ITeS, and financial technology companies called GST Suvidha providers(GSP), who provide mechanism to receive GST returns from the tax payers and forwarding the returns to Central and State authorities;
- b) To develop with the help of GSPs ,applications to be used by taxpayers for interacting with the GSTN and facilitate the tax payers in uploading invoices as well as filing of returns and act as a single stop shop for GST related services;
- c) To customize products that addresses the needs of different segment of users. GSPs may take the help of Application Service Providers (ASPs) who act as a link between taxpayers and GSPs;
- d) To compute and settle IGST with the concerned states/UT,

- e) To match payment of tax by the tax payers with the banking network;
- f) To generate MIS reports from the information furnished by the taxpayers in the GST returns information and provide such reports to the Centre and States,
- g) To analyse and provide analysis of taxpayers' profile;
- h) To match reversal and reclaim of input tax credit.
- i) To ensure data privacy and protection along with developing data retrieval and audit trails and other value added service.

13. SELF-EXAMINATION QUESTIONS

- 1) Explain the concept of GST.
- 2) List the Central and State levies which will be subsumed in GST in India.
- 3) What are the taxes not subsumed in GST
- 4) Enumerate and explain the principles for subsuming taxes in GST.
- 5) What is GST Council: How decisions are made by the GST Council?
- 6) Explain the benefits and need for GST.
- 7) What were the problems in pre-GST tax regime? How does GST resolve them?
- 8) Discuss the dual GST model to be introduced in India.
- 9) Explain salient features of indirect taxes and differentiate direct and indirect taxes.
- 10) Enumerate different types of direct and indirect taxes.
- 11) Write a short note on various Lists under VII Schedule to the Constitution of India.
- 12) If A sells a product at a MRP of 20,000 rupees with VAT rate of 10%. Determine the GST payable. Will it make any difference if A has purchased this product for Rs 15,000?

(Ans. $GST - 20,000 \times 10/110 = Rs\ 1818$, Input credit $15,000 \times 10/110 = Rs\ 1364$, payable $Rs\ 1818 - 1364 = Rs.\ 454$)

13) Multiple Choice questions ;

- A. Which of the following taxes have been subsumed in GST?
 - (a) Central Sales Tax (b) Central Excise Duty (c) VAT (d) All of the above
- B. List I is the - (a) Union List (b) State List (c) Concurrent list (d) None of above

- C. List II is the - (a) Union List (b) State List (c) Concurrent list (d) None of above
- D. List III is the (a) Union List (b) State List (c) Concurrent list (d) None of above
- E. Union list provides taxes levied by
a) Centre (b) states (c) Union territories (d) none of above
- F. State list lists taxes levied by
a) Centre (b) states (c) both centre and states (d) None of above
- G. Concurrent list gives items in the domain of
a) Centre (b) states (c) both centre and states (d) None of above ----
- H. Weight age of Central Govt. in GST Council is a) $\frac{1}{4}$ (b) $\frac{1}{3}$ (c) $\frac{2}{3}$ (d) $\frac{3}{4}$
- I. GST council takes decisions with majority of a) $\frac{1}{4}$ (b) $\frac{1}{3}$ (c) $\frac{2}{3}$ (d) $\frac{3}{4}$
- J. The functions of Goods and Services Network (GSTN) include:
(a) Facilitating registration (b) forwarding the returns to Central and State authorities (c) computation and settlement of IGST (d) All of the above
- K. 3. GST is levied on supply of all goods and services except:
(a) Alcoholic liquor for human consumption (b) Tobacco (c) Health care services (d) All of the above
- L. On Petroleum Crude, High Speed Diesel, Motor Spirit (Petrol), Natural Gas and Aviation Turbine Fuel:
(a) GST is not levied (b) GST to be levied from a notified date decided by GST Council (c) GST is levied, but exempt (d) None of the above

(Answers : (A) c (B) a (C) b (D) c (E) (a) (F) b. (G) (c), H (d), I (d), J (d), K (a), L (d))



REGISTRATION UNDER GST

Synopsis

1. Introduction and Objectives
2. Need and Advantages OF Registration
3. Liability for Registration
4. Registration Procedures
5. Self- Examination Questions

1. INTRODUCTION AND OBJECTIVES

The GST being a destination based tax on the consumer of the goods and services or both; actual taxpayer is different from the factual one. Registration is a process to establish a chain between the Government vis-à-vis the supplier and the consumer. It helps the Government to identify taxpayers and enables the taxpayers to collect tax from the consumers besides establishing a seamless flow for claiming credit of tax paid on inputs (ITC). This lesson takes a detailed look at the provisions relating to Registration, its need, advantages, liability for registration, exemption from registration, procedural aspect for registration and its modification or cancellation etc.

2. NEED AND ADVANTAGES OF REGISTRATION

Primarily, registration is a process for obtaining a unique number from the Government by a supplier of goods or service or both for collecting tax on behalf of the Government and to avail Input tax credit for the taxes on his inward supplies. Without registration, a person can neither collect tax from his customers nor claim any input tax credit of tax paid by him. Registration confers the following advantages to a taxpayer:

- a. Registration is an official recognition to a person as the supplier of goods or services or both.
- b. A registered supplier is authorised to collect tax from the consumers.

- c. The supplier may pass on credit of the taxes paid on the goods or services or both, supplied to the consumers.
- d. The supplier may claim and utilise input tax credit of taxes paid towards the discharge of his liability for taxes due on supply of goods or services or both.
- e. Registration acts as a catalyst in establishing a supply chain at the national level with a seamless flow of Input Tax Credit from suppliers to the consumers.

3. LIABILITY FOR REGISTRATION

Liability for payment of GST arises on happening of the taxable event viz. the “supply” of goods or service or both by a supplier thereof. Liability for registration is co-extensive with the liability to pay GST. A supplier is liable for registration in four ways, viz.:-

- a. Migration of the existing taxpayer from the old law to the GST,
- b. Registration based on minimum turnover of supply of goods or services or both,
- c. Compulsory registration irrespective of the turnover limit, and
- d. Voluntary registration irrespective of the turnover limit.

3.1. Migration of the existing taxpayer from the old law to the GST

The GST came into force on 1st July 2017. Every person who was registered or holding a license under the existing law was required to obtain provisional registration to migrate to the GST by 30th June 2017 i.e. a day preceding the appointed day as per section 22(2) of the CGST Act, 2017. The provisional registration was subject to final registration after submitting the documents and information required for registration. There were elaborate provisions for declaration of stocks and unavailed input credit on 30th June 2017 to facilitate smooth transition to the new regime. This being only a transitory provision, is not discussed in detail.

3.2. Registration based on Turnover of taxable supply

3.2.1. Under section 22 (1) of the CGST Act, 2017, every supplier is liable to be registered under the CGST , in the State or Union Territory, from where he makes a taxable supply of goods or

services or both, if his aggregate turnover in a financial year exceeds the specified limit i.e.:-

- ten lakh rupees in special category states(other than Jammu and Kashmir); and
- twenty lakh rupees in all the other states including Jammu and Kashmir.

As per the section effective threshold limit will be Rupees 10,00,001 / Rs 20,00,001 onwards.

3.2.2. Special category states are Arunachal Pradesh, Assam, Jammu & Kashmir Manipur, Meghalaya, Mizoram Nagaland and Tripura and Himachal Pradesh, Sikkim and Uttarakhand. Jammu & Kashmir, although being a special category state has opted for threshold limit of Rs 20 lakh.

3.2.3. Aggregate turnover

A. “Aggregate turnover” as defined in section 2(6), means the aggregate value of-

- i. all taxable supplies,
- ii. exempt supplies,
- iii. exports of goods or services or both, and
- iv. inter-State supplies

B. Aggregate turnover of supply of goods or services or both is computed :-

- a. for a supplier having the same Permanent Account Number, on the principle of one PAN- one person,
- b. for the whole of India taken together,
- c. with reference to a financial year i.e. April to March

C. The value of aggregate turnover **excludes:-**

- a. Central tax, State tax, Union territory tax, Integrated tax and Cess;
- b. The value of inward supplies on which tax is payable by a person on reverse charge basis;

D. vide explanation to the section 22 , the aggregate turnover **includes:-**

- a. all supplies made by the taxable person on his own account ; or
- b. supplies made on behalf of all his principals; or
- c. in case of a principal, the supply of goods by a registered job worker after
- d. completion of job-work,

3.2.4. Persons not liable for registration-Section 23

Following persons are not liable for registration vide Section 23 :-

- A. Any person engaged **exclusively** in the business of supplying goods or services or both; that are not liable to tax or wholly exempt from tax under the CGST Act or under the IGST Act;
- B. an agriculturist, to the extent of supply of produce out of cultivation of land
- C. Any class of persons specified by the Government on the recommendations of the Council, by notification. Under this section, the government has granted exemption from registration under this section, to :
 - (i) Individual advocates including senior advocates ,
 - (ii) Individual sponsorship service providers including players ,
 - (iii) *Suppliers, whose all supplies are taxable under reverse charge (vide Notification No. 5/2017-Central Tax dated 19.06.2017).*

3.2.4. Some relevant points

From the above, the following points emerge out, namely:-

- a. The liability for registration is on “every supplier”.
- b. The supplier should make a taxable supply of (i) goods or (ii) services or (iii) both over the threshold limit of 10 lakh/20 lakh rupees.
- c. Under section 22 read with section 23, a supplier of only tax-free supplies is not liable for registration but if he some taxable supply, then, all supplies, whether taxable or tax-free in the course of export or inter-State supply, will be considered in aggregate turnover.
- d. Registration will in the state or union territory, from where the supplier makes the taxable supply of goods or services or both.
- e. An agriculturist is specifically exempted from registration to the extent of supply of produce out of cultivation of land, even if exceeds the threshold limit.
- f. Similarly a supplier of only supplies taxable under reverse charge, is also exempted from registration vide Notification No. 5/2017-Central Tax dated 19.06.2017.
- g. All supplies by a taxable person will be included in his aggregate turnover whether made
 - on his own account; or
 - as an agent on behalf of all his principals; or

- in case of a principal, the supply of goods, after completion of job-work, by a registered job worker.
- h. The value of the supply considered in the account of the principal, shall not be included in the aggregate turnover of the registered job worker because only one person should be liable for accounting the turnover of supply.

3.2.5. Illustrations:

1. A is chartered accountant providing taxable services from Agartala. He will be liable for registration u/s 22, when the value of services provided by him exceeds Rs 10 lakh applicable to the state of Tripura, a special category state.
2. B is a Kolkata based wholesaler in tea. He will be liable for registration, when the aggregate turnover or supply of tea (sales) exceeds Rs 20 lakh.
3. S of Surat supplies (sells) taxable goods worth Rs 18 lakh on his account and Rs 3 lakh as an agent acting for his principal T. S will be liable for registration, when the turnover exceeds Rs 20 lakh inclusive of supply made on his account and made on T's account.
4. D is a diamond merchant of Mumbai. D has turnover of Rs 5 lakhs and he sends goods on job work to the registered artisan. The artisan completes the job work and sends goods to D valued at Rs 25 lakh. S will be liable for registration on his own turnover and the goods received from the job worker, when the turnover exceeds the threshold limit of Rs 20 lakh. However, then the turnover of Rs 25 lakh will be excluded from the turnover of the job worker.
5. An educational institution provides tax- free education services valued at Rs 50 lakh. It will not be liable for registration u/s 23 because it does not provide any taxable supply.
6. A hospital provides tax-free medical services of Rs 18 lakh and taxable services of Rs 4 lakh. It will be liable because its aggregate turnover exceeds Rs 20 lakh.
7. A makes export of taxable goods for Rs 100 lakh. A will be liable for registration, although his tax liability will be nil.
8. A of Akola is engaged exclusively in supplying tax-free goods. He is not liable for registration under this clause even of the turnover exceed the limit of Rs 20 lakh.
9. Turnover of B of Bengaluru from supplying exempted goods is Rs 50 lakh and on supplying taxable goods is Rs 25 lakh. B will be liable for registration from the date on which the aggregate turnover of supply of goods exceeds Rs 20 lakhs.

3.3. Compulsory registration

Following categories of persons are liable for compulsory registration under section 24 of the CGST Act, 2017, irrespective of the amount of turnover:-

(i) Inter-State Suppliers

Persons making any inter-State taxable supply (e.g. from Mumbai to Goa); However, persons making inter-State supplies of taxable services and having an aggregate turnover, to be computed on all India basis, not exceeding an amount of twenty lakh rupees (ten lakh rupees for special category States except J & K) are exempted from obtaining registration vide Notification No. 10/2017-Integrated Tax dated 13.10.2017.

ii) Casual taxable persons

A casual taxable person is one who has a registered business in a different State and wants to affect taxable supplies from some other State or Union Territory where he is not having any fixed place of business. Such persons are liable for registration in the State from where they seek to affect a taxable supply as a casual taxable person.

An exception is made in case of casual taxable persons making supplies of specified handicraft goods, who will be entitled to the threshold exemption of Rs. 20 Lakh/10 lakh and thus need not take compulsory registration.

(ii) Non-Resident Taxable Persons

Non-resident taxable persons i.e. a foreigners not having fixed place of business in India has to compulsorily apply for registration if they desire to make any taxable supply any State in India at least five days in advance of making such supply and also make advance deposit of the estimated tax liability. Registration is granted to the non-resident taxable persons only for a specified period only, but the period may be extended on making application.

(iii) Payers of tax under reverse charge

The persons who are required to pay tax under reverse charge on the supplies received by them. e.g. clients of advocates, those receiving transport services from a goods transport agency etc.

(iv) E-Commerce Operators

E-commerce operators, notified as liable for GST payment under section 9(5) of the CGST Act, 2017.

(v) Tax Deduct or;

Persons required to deduct tax under section 51, whether or not separately registered under this Act;

(vi) Agents

Persons making taxable supply of goods or services or both on behalf of other taxable persons whether as an agent or otherwise;

(vii) Input Service Distributors, whether or not separately registered under this Act;**(viii) Suppliers through E-Commerce Operator subject to TCS**

Persons who supply goods or services or both, other than supplies specified under section 9(5) through such E - Commerce Operator who are required to collect tax at source(TCS) under section 52;

(ix) Supplier through E- Commerce Operators subject to TDS

Suppliers of goods who supply through such E-Commerce Operators, who are liable to collect tax at source. However , suppliers of taxable service through e-commerce operators need not take compulsory registration and are entitled to avail the threshold exemption of Rs. 20 lakh/10 lakh(Notification No. 65/2017-Central tax dt. 15.11.2017)

(x) E-commerce Operators, who provides platform to the suppliers to make supply through them.**(xi)** Every person supplying Online Information and Database Access or Retrieval Services (OIDAR) from a place outside India to an unregistered person in India.**(xii)** Such other person or class of persons as may be notified by the Government on the recommendations of the Council.**3.4. Voluntary registration**

Any person having turnover below the threshold limit can apply for voluntary registration. Such a person will not get the benefit of the threshold limit of Rs 20 lakh /10 lakh. Their entire turnover will be subject to GST from the day of registration. Further a voluntary registration will not be cancelled until one year from the date of registration.

4. REGISTRATION PROCEDURES

There are different procedures for registration for a non-resident taxable person, casual taxable persons, deductors of tax, collectors of tax and supplier of Online Information Database Access and Retrieval (OIDAR) services and other suppliers. Some relevant provisions have been dealt with separately at the appropriate places. For all other suppliers the following will be the procedure for registration.

4.1. Nature of Registration

- (i) Registration under GST is not tax specific. There will be a common registration for all the taxes i.e. CGST, SGST/UTGST, IGST and Cesses.
- (ii) Registration under GST is PAN based and State specific. A given PAN based legal entity would have one GSTIN per State. It would mean:-
 - i. A taxable person is required to register in each State or Union territory from where he effects supply. Hence, an entity having branches in multiple States will have to take separate State wise registration for the branches in different States.
 - ii. If the branches of the entity are within one State or Union territory, it can have single registration declaring one place as the principal place of business and other as the branches as additional place of business.
 - iii. The above rule subject to the following three exceptions , where separate registration is required even within a state :
 - a) a unit in SEZ ; or
 - b) a SEZ developer; or
 - c) Each of business verticals separately of business entity within a State or Unit Territory. Section 2 (18) of CGTS Act, 2017 defines business vertical as under:
 “business vertical means a distinguishable component of an enterprise that is engaged in supplying an individual product or service or a group of related products or services and that is subject to risks and returns that are different from those of other business verticals;

Explanation: Factors that should be considered in determining whether products or services are related include:

- (a) the nature of the products or services;
 - (b) the nature of the production processes;
 - (c) the type or class of customers for the products or services;
 - (d) the methods used to distribute the products or provide the services; and
 - (e) if applicable, the nature of the regulatory environment, for example, banking, insurance, or public utilities.”
- iv. Upon registration each supplier is allotted 15-digit ‘ Goods and Service Tax Identification Number or “GSTIN” comprising of the first 2 digits for the State code followed by 10 digits PAN of the legal entity, 2 digits for the entity code and the last digit for check number.
 - v. A centralised unique identification number (UIN) is issued in respect of supplies to some notified agencies of United Nations organisation, multinational financial institutions and other organisations.
 - vi. Upon Registration a certificate of registration incorporating the GSTIN is issued to the taxpayer and the GSTIN is made available to the applicant on the GSTN common portal.

4.2. Standardisation of procedures for Registration

The GST registration rules prescribe as many as 30 standard forms / formats to be used for every process in the registration chain such as application for registration, acknowledgment, query, rejection, registration certificate, show cause notice for cancellation, reply, cancellation, amendment, field visit report etc., This is to ensure uniformity of the process all over the country and speeding up the decision making process. Further, the rules stipulate strict timelines for completion of different stages of registration process. The standardized process for Registration is given below.

I. Procedure for Registration Regular Taxpayers

A. Submission of Application for Registration

- (i) Every taxable person, who is not a non-resident, deduct or of tax and collector of tax has to submit application for registration

online through the common portal (GSTN) or the Facilitation Centre in form GST REG-01.

- (ii) Time limit for submission of application is within thirty days from the date when liability to register arose
- (iii) Form for GST REG-01 is in two part – Par A and part B
 - (i) Part- 'A' – contains the applicant entity's name PAN, Mobile, email etc.
 - (ii) Part - B application reference no. given in acknowledgment in GST-REG-02.
- (iv) Following documents are required for GST registration :-
 - (i) PAN of the applicant
 - (ii) Identity and address proof of the promoters.
 - (iii) Proof of registration of business, e.g. partnership deed, registration certificate, certificate of incorporation etc.
 - (iv) Address proof for place of business such as Rent receipt, electricity bill, Municipal certificate etc.
 - (v) Bank account proof.
 - (vi) Digital Signature.
- (v) On submission of the application, PAN of the applicant is verified through GST portal Mobile no. and PAN through One Time Password (OTP) and if these documents are found to be in order, an acknowledgment will be issued in Form GST-REG-02 electronically.

B. Verification process

- (i) The application will be forwarded to the Proper Officer of the respective State or the Central Government, who shall examine the application and the accompanied documents and after the verification, the Proper Officer shall approve and grant the registration within three working days.
- (ii) Where, the Proper Officer finds the application to be deficient for any reason or requires any further clarification, he shall intimate to the applicant in form GST-REG-03.
- (iii) The applicant shall submit the reply with clarification in form GST-REG-04 within seven working days starting from the fourth day of filing the original application/ the date of receipt of

such information in form GST-REG-03. The clarification includes modification or correction of particulars declared in the application for registration.

C. Grant or Refusal of Registration

(i) The proper officer would have to grant the application for registration within seven working days thereafter and

a) issue Registration Certificate in form GST-REG-06 or

b) reject the application in form GST-REG-05.

(ii) If the proper officer does not respond within 3 working days of receipt of application or within 7 working days from receipt of clarification, then application under this Act shall be deemed to have been approved.

D. Physical verification in connection with registration

The basic premise of the GST is reduction of physical interface and evolve a technology based tax regime. Hence, physical verification is avoided. However, where the Proper Officer is satisfied and deems necessity or desirable to carry out physical verification, he may do so only after granting the registration. Further after the verification, he shall upload the verification report along with the supporting documents and photographs to on the common portal within fifteen working days.

II. Registration procedure for Casual Taxable Persons

(i) Registration under GST is compulsory for the casual taxable persons irrespective of the annual aggregate turnover. For this purpose

- A casual taxable person as a person who occasionally undertakes transactions involving supply of goods or services or both in the course or furtherance of business, whether as principal, agent or in any other capacity, in a State or a Union territory where he has no fixed place of business. Persons running temporary businesses like event management, business fairs or exhibitions or other seasonal businesses fall under casual taxable persons under GST. Casual taxable, unlike the regular taxable person do not have a fixed place of business located in a State or Union Territory where they supply of goods or services or both.

(ii) A Casual Taxable person shall make the application for GST registration in form GST REG-01 at least 5 days prior to the commencement of business.

(iii) Deposit for GST Registration

A Casual Taxable person can not opt for composition scheme. Instead, he will have to deposit an amount equivalent to the expected tax liability during the validity period of GST registration in advance for GST registration. For this purpose, a temporary reference number is generated for payment of GST deposit.

(iv) On paying the GST deposit, the electronic cash ledger of the taxpayer is credited, and GST registration certificate is released, which will be valid initially for a period specified in the application or 90 days, whichever is earlier.

(v) The period of extension may be extended for a further period of 90 days on making application in form -GST-REG-11 before the expiry of the original validity period of registration and amount of additional tax liability during the extended period will have to be made. Other procedures will be similar as those applicable *mutatis mutandis* to regular taxable persons

(vi) Filing of returns:

A registered a casual taxable person has to file the following monthly returns

- Form GSTR-1 on or before the 10th of the following month giving detail of the outward supplies of goods or service made by him
- Form GSTR-2 after the 10th but on or before the 15th of the following month giving detail of the inward supplies made by him
- Form GSTR-2 after the 15th but on or before the 20th of the following month showing the tax liability base on auto populated details of GSTR 1 & 2.
- There is no requirement for filing annual return by a casual taxable person.

(vii) Refund of Tax

After filing all the returns for the registration period, a refund may be claimed in GSTR-3 and allowed in respect of the excess tax paid by the causal taxable person.

III. Registration procedure for Non- Resident Taxable Persons

(i) Registration under GST is compulsory for the casual taxable persons irrespective of the annual aggregate turnover or any other criteria. For this purpose:

- A Non-resident taxable person means any person or business or not-for-profit Organisation who occasionally undertakes transactions involving supply of goods or services or both, whether as principal or agent or in any other capacity, but who has no fixed place of business or residence in India. Foreigners and foreign entities supplying goods or services to India will be non-resident taxable persons as per the GST.

(ii) A Non-Resident Taxable person shall identify a person in India to act as its authorised representative who shall be a person resident in India having a valid PAN.

(iii) Application for registration shall be submitted

- at least 5 days prior to the commencement of business in India ,
- shall be in form GST REG-09, and
- signed by his authorized signatory having a valid PAN in India

(iv) the non-resident taxable person during the GST registration process must file the following documents :

- documents showing Proof of Principal Place of Business(Rent receipt agreement, electricity bill etc. or consent letter from the owner of the premises),
- Identity proof of the non-resident taxable person - Passport, Visa etc.,
- Tax identification number or unique number on the basis of which the entity is identified by the Government of that country or its PAN, if available,
- Authorisation for Authorised Representative in India along with the copy of the resolution of the board of directors granting such Authorisation, if any
- Certificate of Incorporation of the Company.
- License issued by foreign country, if any
- Clearance certificate issued by Government of India, if any, and
- Bank Account Proof with IFC Code MICR etc.

(v) GST Deposit for Non-Resident Taxable Persons

Like the Casual taxable persons, Non-resident taxable persons are required to remit in advance a deposit equivalent to the expected tax liability during the validity of the registration for GST registration, where upon the registration certificate will be issued. Similar process is to be followed for extension of restoration period and additional deposit will be required to be made equivalent to the estimated tax liability for the extended period. An application reference number would be generated for payment of advance tax for obtaining GST registration and an allocation will have to be filed for extension of registration Period in for GST-REG-11. .

(vi) For final registration , an application is required to be submitted in form GST REG-26 electronically within a period of 3 months from the provisional registration Other provisions are similar to those applicable on the regular taxable persons in regard to the final registration

(vii) The proper officer, after verification shall issue registration in form GST REG-06.

(viii) If the officer is not satisfied with the correctness or completeness of the information submitted or needs additional information, he shall issue a show cause notice to the applicant in Form GST REG-27.

(ix) If the reply to the show cause is satisfactory, the show cause notice may be cancelled by issuing an order in Form GST REG-20, and if it is not satisfactory, then the officer after giving opportunity of being heard to the applicant may pass an order for cancellation of the provisional registration granted to the applicant in Form GST REG-28.

(x) The rules for filing of returns, refunds etc. are similar to those applicable to the casual taxable persons.

IV. Registration Procedure – OIDAR Service Providers

A taxable person supplying online information and data base access or retrieval (OIDAR) services to a non-taxable online recipient shall file the application for registration in Form GST REG-10 electronically and follow the procedure applicable to non-taxable persons.

V. Registration Procedure – Deduct or collector of GST

A person who is liable to deduct GST at source or collect GST e.g. e-commerce operator will have to follow the normal procedure as applicable except that application for registration shall be submitted electronically in Form GST REG-7

VI. Registration Procedure – Special agency like United Nations.

United Nations and other connected specified agencies shall apply for registration in GST-REG-13. It may be noted that these agencies are not liable to GST under the international protocol, but registration will still be required to claim refund of taxes paid on inward supply of goods or service or both.

VII. Succession or Transfer of Business

Liability to registration is on the transferee of a business as going concern as result of succession or transfer of business as result of amalgamation, merger, demerger, or change in constitution etc. from the date of transfer or succession and the transferee has to follow the applicable procedure as above.

4.3. Amendment of Registration

Amendment in particulars of registration may be for the three reasons, viz. :

(i) Change in Core field

Under Rule 12, a taxable person may make an application for amendment in Form GST - REG -14 within 15 days of the following changes, which do not require cancellation under section 29 of CGST Act,

- (i) legal name of the business, or
- (ii) the State of place of business or
- (iii) additional place of business., or
- (iv) names of the functionaries – like partners , directors , etc

The proper officer shall after making necessary inquiry, approve the amendment electronically in form GST -REG-15 within next 15 days from the date of application.

(ii) Change in Non- Core field

All the other corrections amendments or change in the particulars of registration are called the change in non- core field. A taxable person *suo motu* (on his own) may effect the change on the common portal without seeking approval of the proper officer. This change includes a change in the name of the authorised signatory by adding another name of signatory; otherwise the change will not be effective.

(iii) Change in Mobile, email etc.

Change in e mail, or mobile numbers may be effected in the common portal by the taxable person after an online verification through One Time Password is issued.

iv) Eligible persons

A tax payer may also change in the particulars can be effected by the following categories of persons, viz:

- (i) Applicant, Taxable person
- (ii) Person holding UIN Card or other notified person for registration under TDS/TCS U. N. bodies category,
- (iii) Non-Resident taxpayer
- (iv) GST Practitioner, and
- (v) Online application and retrieval service provider.

Fields, which cannot be changed

GST is State specific PAN based, hence the following changes which have the effect of changing these particulars is not allowed. E.G.

- a. PAN details
- b. Change in constitution of business ,
- c. Modification of place of business from one state to another.
- d. In these cases, a fresh registration will have to be obtained after canceling the existing registration.

The amendments will come into effect from the date of application for amendment.

However, the Commissioner may allow the amendments with retrospective effect.

4.4. Cancellation of Registration

4.4.1 Under section 29(1), registration can be cancelled only in two circumstances :-

- (i) Voluntary cancellation when a taxable person no more requires it , or
- (ii) the Proper Officer considers the registration liable due to some specific defaults.

4.4.2. Voluntary Cancellation :

a) Cancellation of Registration of Migrated Taxpayers :

A taxpayer, who has migrated from old tax to GST, may opt for cancellation

- on GSTN portal online, if he has not issued any tax invoice , or
- in Form GST- REG- 16 if his issued any tax invoice.

In either case, cancellation is allowed only for the following reasons :-

- a) turnover is below the threshold limit , or
- b) his supply is in exempted category.

b) Cancellation of Registration of Other Taxpayers

1. Time condition

- (i) Where a taxable person not being liable for obtaining registration, has taken voluntary registration, cancellation of registration is not allowed until expiry of one year from the effective date of registration.
- (ii) Other taxpayer may opt for cancellation anytime as the condition of one year does not apply on them.

2. Reasons for cancellation

The cancellation may be for the following reason:-

- a) the business of the taxpayer has been discontinued ; or
- b) the business has been sold or transferred to some other entity and that other entity needs to register under GST; or

- c) turnover is below the threshold limit , or
- d) the supply is in exempted category.

3. **Procedure for cancellation**

A taxable person desirous of cancellation of registration may apply on the common portal within 30 days of event warranting cancellation in Form GST-REG-16. Such person is required to :-

- a) declare in the application the stock held on the date with effect from which he seeks cancellation ,
- b) work out and declare:-
 - the quantum of dues of payments,
 - credit reversal, and
 - the particulars of payments made towards discharge of such liabilities.

4. On receipt of the application the Proper officer shall cancel the registration within 30 days from the date of application or receipt of explanations or clarifications in response to his notice issued by him in Form GST-REG-16, if any. The notice has to be replied in Form GST-REG-18 within seven days. The order of cancellation in will be in Form GST-REG-19. Revocation of notice will be in Form GST-REG-20.

C. Suo-motu cancellation by the Officer

The Proper Officer may issue a show cause notice in Form GST-REG-16 to a registered person and call for information and after considering such information and hearing the taxpayer , cancel the registration by passing an order in Form GST-REG-19, if he is satisfied that the registered person has :

- (i) contravened the provision of the Act and the Rules;
- (ii) furnished returns for-
 - a) three consecutive tax periods in case of a composition taxpayer , or
 - b) Continuous period of six month in case of a regular taxpayer ;

- (iii) obtained voluntary registration but not commenced business within six months of registration;
- (iv) obtained registration by means of fraud, willful misstatement or suppression of facts;
- (v) discontinued business from the registered place of business;
- (vi) been issuing tax invoice without making the supply of goods or services; or
- (vii) Committed such other defaults as may be specified.

4.5. Revocation of Cancellation

Where registration is cancelled suo-motu, the taxable person, within a period of 30 days the service of cancellation order, may apply to the Proper Officer for revoking the cancellation order.

No such application shall be entertained unless the taxable person, before making such application, has made good the defaults by filing all pending returns, making payment of all dues etc. for which the registration was cancelled by the officer.

On receipt of the application, the Proper Officer, if satisfied, may either revoke the cancellation earlier ordered by him or reject the request for revocation of cancellation, after observing the principle of natural justice by way of issuing notice to the person and hearing him on the issue.

4.6. Cancellation not to affect pending tax liability :

Cancellation of registration will not affect the liability of taxes prior to cancellation. Further, the taxpayer will have to pay his due taxes by reversing the input credit in stock (Raw materials, finished or semi-finished goods) or make payment, whichever is higher. Similarly, input credit on capital goods also will have to be reversed or the payment will have to be made.

5. SELF EXAMINATION QUESTIONS

1. Explain the concept of Casual Taxable person.
2. What are the provisions for registration of a non-resident taxable person?
3. List out the forms used for registration and cancellation
3. State whether the following are true or false:

- a) A migrated person cannot cancel his registration
- b) Registration may be refused if turnover does not exceed the taxable limit
- c) A farmer is not liable to GST in respect of his agriculture
- d) A plastic surgeon, who provides life-saving surgery for Rs. 10 lakh (exempt) and cosmetic surgery (taxable) for Rs 12 lakh not liable for registration.
- e) A charitable trust is not liable for registration under GST.
- f) An advocate is liable for registration under GST.
- g) A Jammu taxpayer with taxable turnover of Rs. 15 lakh not liable for registration.
- h) Application for registrant in is to be made in GST-REG 1
- i) A non- resident has to pay tax in advance
- j) A GST number taken by fraud can be cancelled
- k) A cancellation order can not be revoked.

(False a, b, d, e, f and j , True c, g, h, i)



PLACE OF SUPPLY UNDER IGST

Synopsis

1. Introduction and Objective
2. Inter -State Vs. Intra-State Supply
3. Location of the Recipient of services
4. Location of the Supplier of services
5. Place of supply in respect of goods and services
6. Place of supply in respect of goods
7. place of supply in case of supply of services, when location of the supplier and recipient is in India
8. place of supply in case of supply of services, when location of the supplier and recipient is in India
9. Self- Examination Questions

1. INTRODUCTION AND OBJECTIVE

Determination of the place of supply of goods and/or services is of great importance as the GST being a destination based tax is levied at the place, where the goods and/or services are consumed, not at the place of origin. Accordingly, each transaction has to pass through the test of the place of supply to determine: -

- a. whether tax is to be levied on a particular cross-border transaction;
- b. whether a particular transaction it is an Inter-state supply or Intra-state supply;
- c. who will collect the tax on such transaction; and
- d. type of the tax is be levied; IGST, CGST, or SGST/UTGST, on that transaction.

Further, the Place of supply depends upon the location of the recipient of services and the location of the supplier of services. This lesson will deal with the provisions relating to the place of supply of goods and their implication

2. INTER-STATE SUPPLY VS INTRA-STATE SUPPLY

2.1. Broadly, the transactions may fall in two categories: -

- A. International or cross border transactions, viz.:
 - a. Imports of goods into India; or
 - b. Export of goods outside India, and
- B. Domestic transactions, viz:
 - a. Inter-state supply
 - b. intra-state supply

2.2. Inter-state supply is when “location of supplier” and “place of supply” are in different States or Union Territories (section 7 of the IGST Act). In contrast, intra-state supply is when “location of supplier” and “place of supply” are in the same state or same union territory (section 8 of the IGST Act).

Examples

1. A supplier in Gujarat sells good in Gujarat. It is intra-state supply, liable to CGST and SGST as location of the supplier and the place of supply are within the same state (Gujarat).
2. The supplier in Gujarat sells goods in Goa. It is an inter-state supply attracting IGST as the location of the supplier and the place of supply fall in different states.

While, Section 2(70) and 2(71) of CGST Act define “location of the recipient of services” and “location of the supplier of services” respectively, the Act does not define “location of the recipient of goods” and “location of the supplier of goods” at any place.

3. “LOCATION OF THE RECIPIENT OF SERVICES

As per section, 2(70) of CGST Act, 2017, “location of the recipient of services” means, —

- (a) where a supply is received at a place of business for which the registration has been obtained, the location of such place of business;
- (b) where a supply is received at a place other than the place of business for which registration has been obtained (a fixed establishment elsewhere), the location of such fixed establishment;
- (c) where a supply is received at more than one establishment, whether the place of business or fixed establishment, the location of the establishment most directly concerned with the receipt of the supply; and

- (d) in absence of such places, the location of the usual place of residence of the recipient;

Thus, the location of the recipient primarily means: -

Supply Received at	Location of Recipient of Service
Place of business for which the registration has been obtained	Recipient's Registered Office;
Place other than the place of business for which registration has been obtained, a fixed establishment	Recipient's fixed establishment
at more than one establishment, whether the place of business or fixed establishment	the location of the establishment most directly concerned with the receipt of the supply
in absence of such places	the location of the usual place of residence of the recipient;

Illustration:

A is registered at Fort, head office at Dadar and branches at Thane and Borivali. His residence is in Juhu.

For any supply received in Thane office, the place of recipient will be at:

1. registered office at fort,
2. Dadar office, if A does not have registration at fort; or
3. Most connected office at Thane (in absence of fort and Dadar offices, and
4. Residence at Juhu, in absence of any of the above.

4. "LOCATION OF THE SUPPLIER OF SERVICES"

U/s section 2(71), of the CGST Act, "location of the supplier of services" means: —

(a) where a supply is made from a place of business for which the registration has been obtained, the location of such place of business;

(b) where a supply is made from a place other than the place of business for which registration has been obtained (a fixed establishment elsewhere), the location of such fixed establishment;

(c) where a supply is made from more than one establishment, whether the place of business or fixed establishment, the location of the establishment most directly concerned with the provisions of the supply; and

(d) in absence of such places, the location of the usual place of residence of the supplier;

The yardstick for determining the location of the provider or supplier of service are more or less similar to those applicable on location of the receiver of the supply.

Supply made from	Location of Supplier of Service
Place of business for which the registration has been obtained	Recipient's Registered Office;
Place other than the place of business for which registration has been obtained, a fixed establishment	Recipient's fixed establishment
at more than one establishment, whether the place of business or fixed establishment	the location of the establishment most directly concerned with the provision of the supply
in absence of such places	the location of the usual place of residence of the supplier

Example:

Goods are supplied to Jamnagar Branch of Reliance Industries Limited. Its registered office is in Surat and the corporate office is in Mumbai. Place of supply will be Surat, Mumbai and Jamnagar in that order.

5. PLACE OF SUPPLY OF GOODS AND SERVICES

Section 10 and section 12 of the IGST Act, 2017 lay down the principles for determination of place of supply broadly in three categories viz.: -

Section 10	Supply of goods
Section 12	Supply of services where location of both the supplier and the recipient is in India;
Section 13	Supply of services, where location of either the supplier or the recipient is outside India.

6. PLACE OF SUPPLY IN RESPECT OF GOODS

Section 10 of the IGST, Act, 2017, lays down the following principles to determine place of service of goods

4.1. When there is movement of goods

When there is movement of goods, there may be two situations: -

A. Where supply involves movement of goods whether by the supplier or the recipient or by any other person, place of supply is the place where the movement terminates i.e. where the goods are delivered or the ownership in goods is transferred.

Examples

1. Ashok of Akola sells 100 cotton bales to Ramesh of Dhule. The place of supply is Dhule in Maharashtra, where the movement of goods is terminated. Both Akola and Dhule being in the same state Maharashtra, it is intra-State sales liable to CGST & SGST.

2. If Ashok sells goods to Rajesh of Bhopal in M.P., the place of supply will be in Bhopal M. P. M.P. and Maharashtra being different states; it will be inter-state sales attracting IGST.

3. P of Pune places an order to Reliance, Surat (Gujarat) for purchase of mobile phones goods ex-factory.

Surat will be the place of supply as the goods are delivered there. Both, the place of supply and location of the supplier being in same State Gujarat, it will be intra-State sales chargeable to CGST and SGST. It is immaterial that P after collecting goods from the factory of Reliance Surat transports the goods to his place of business in Pune or anywhere else.

B. Delivery to a third party as per instructions

When goods are delivered by a seller to the recipient (whether agent or not) on the direction of a buyer before or during the movement of goods, by way of transfer of document of title to the goods or otherwise, the place of supply will be the principal place of the buyer on the assumption that the buyer has received the goods.

Examples

1. Rakesh of Ranchi buys umbrellas from Mahesh of Mumbai to be delivered to his father living in Mumbai.

When the umbrellas are delivered in Mumbai (to his father), it will be assumed that Rakesh has received the goods at his principal place in Ranchi. Place of supply is in Ranchi (Jharkhand) Ranchi and Mumbai (Maharashtra) being different states, it will be inter-State sale Chargeable to IGST.

2. Raju of Mumbai places an order for a watch on Snapdeal (an e-commerce operator) manufactured by Foss Ltd., Bengaluru (registered with Snapdeal) to be delivered to Rakhi, his sister in Delhi.

This is again a case of delivery of third party. Delivery of watch to Rakhi in Delhi will be assumed to be delivery to Raju at his principal place in Mumbai by the Supplier Foss (Bengaluru).

Karnataka). Hence, Mumbai will be the place of supply and as inter-State sales, IGST will be chargeable.

4.2 When there is no movement of goods

A. Where supply does not involve movement of goods, the place of delivery of goods will be the place of supply.

Examples

1. A of Mumbai has goods stored in B's godown in Pune. A sell these goods to B.

Place of service will be in Pune, when B appropriates the goods although there is no physical movement of goods. This being intra-state as the supplier and the place of supply both are in the same state CGST and SGST will be charged.

2. If A of Mumbai sells good lying in Jaipur to B of Jaipur, the place of delivery will be Jaipur. The place of supply Jaipur and the location of the supplier A (Mumbai) being in different states, IGST will be charged.

3. Bhansali, a Mumbai based film producer purchases a studio in Ramoji Rao Complex in Hyderabad with pre-installed audi-visual equipments. The place of supply is Hyderabad being the location of equipments at the time of delivery along with the studio building, which is same as the location of the supplier. Hence, CGST and SGST will be charged as intra -State sale. There is no GST on sale of building being a capital asset.

B. The goods assembled or installed at site

Where, goods are assembled or installed at the site of the buyer, site will be the place of supply.

Example

L &T Ltd., Mumbai fabricates oil storage tank at a Refinery in Odisha.

The place of supply is Odisha, where the oil storage tank is installed or fabricated. This being an inter-State sale from Mumbai (Maharashtra) to Odisha, IGST will be charged. However, L &T may apply for registration as casual taxable person in Odisha and pay CGST & SGST.

C. Goods Supplied on a Vessel/Conveyance

Where the goods are supplied on board a conveyance including any vessel, aircraft, train or a motor vehicle, place of supply is the location where such goods are taken (loaded) on board.

Examples

1. A buys food articles on board while travelling from Mumbai to Delhi by air.

Mumbai is the place of supply since the food items are loaded into the plane in Mumbai. If the Airline is registered in Mumbai, CGST & SGST will be charged. But if the Airline is registered in Delhi, IGST will be charged. (Ordinarily CGST/SGST is charged as most Airlines are registered across the country).

2. Kamal, a consultant for JW Ltd, Delhi buys food articles on board, while flying from Chennai to Bengaluru.

CGST & SGST will be charged as inter- State sales in Chennai being the place of supply, where the food articles were loaded.

3. Vinod is travelling from Bhopal (M. P.) to Kolkata by Gitnajali Express starting from Mumbai. Vinod buys lunch on board at Raipur in Chhattisgarh. The Lunch was loaded by the IRCTC in Nagpur (Maharashtra).

The food items were loaded in Nagpur, hence place of supply is Nagpur. Since IRCTC is registered throughout India, CGST & SGST will be charged

Where place of supply can not be determined, Parliament will make rule on the recommendation of GST Council.

- D. Where, supply is by transfer of documents, place of supply will be the principal place of business of the person receiving the supply.

Example

A of Delhi sells goods by endorsing airways bill for goods lying in Mumbai, from where the buyer takes the delivery of the goods. The place of supply is in Mumbai by a supplier in Delhi. It will be inter-state sales and CGST and SGST will be charged.

- E. In case of import of goods into India, place of supply is location of the importer and IGST will be charged?

Example

A toy dealer having his principal office in Pune imports Chinese toys in Mumbai port.

Place of supply is Pune and IGST will be charged on the value of imports

F. In case of export of goods outside India, place of supply is outside India. Exports are exempt from GST.

Example 2

A of Allahabad exports garments from Kolkata airport to Italy.

Place of supply will be in Kolkata. Exports are exempt from GST.

7. PLACE OF SUPPLY IN RESPECT OF SERVICES WHEN LOCATION OF THE SUPPLIER AND RECIPIENT IS IN INDIA

Section 12 of the IGST Act spells out the principles for determination of place of supply in case of supply of services, when location of the supplier and recipient is in India, which are as under:

1. General Rule

Where the services are provided to a registered person, place of supply of services is place of location of the registered recipient of services.

Example

A computer mechanic provides services to a chartered accountant registered in Mumbai. Place of service will be in Mumbai.

2. If the recipient is not registered, place of supply is address on record of the recipient.

Example

A computer mechanic provides services to a chartered accountant in Mumbai, who is not registered and his address on record is at Pune

Place of service will be at the address on record (i.e. Pune)

3. In other cases, it is location of supplier of services.

4. Immovable Properties _ Architects, surveyor etc.

Place of supply of services in case of services related to immovable property like architects, interior decorator, property agents, surveyors, engineers, hotels, inns, guest houses, lodges, club, banquet halls etc. shall be the location of the immovable property.

Example

An U.S. Architect makes designs and plans for Trump Tower in Pune. Place of service shall be Pune as the service is related to immovable property located in Pune

5. Performance based service

In case of restaurant and catering, personal grooming services like beauty treatment, health, fitness etc. shall be the place of performance of these services.

Example

A bridal makeup artist of Mumbai goes to provide service in wedding in Delhi. Place of service will be Delhi, where the grooming service was provided.

6. Transport & Insurance etc.

Several services such as transportation of goods, transportation of passengers, Insurance etc, place of supply shall be the location of registered person.

7. Banking Services

In case of banking, place of supply is location of the recipient on record.

8. Telecommunication services

In case of telecommunication services involving fixed line, circuits, dish etc., place of supply is location of such fixed equipment.

Example

In respect of set top box fixed at the homes of viewers, place of service will be at the place where such box is installed.

9. Mobile / Internet Services

In case of mobile/ internet post-paid services, Place of service is location of billing address of the recipient.

In case of sale of pre-paid voucher, place of supply is place of sale of such vouchers.

In other cases, it is address of the recipient in records.

Examples

1. Billing Address for mobile phone of X a resident of Thane is his Pune address. Place of service shall be Pune.
2. Y has purchased an Airtel prepaid talk-time voucher in Delhi. Place of service shall be Delhi even if he is resident of Chandigarh.

8. PLACE OF SUPPLY OF SERVICES WHEN LOCATION OF EITHER THE SUPPLIER OR THE RECIPIENT IS OUTSIDE INDIA – SECTION 13

International Transactions

These are the transactions where either of the service recipient or the provider is outside India. Transactions, in which both the recipient as well as provider are outside India are not covered. In such a transaction, place of service will be determined as per section 13 of IGST, Act, 2017. The section provides several principles for determination of place of service as given below.

A. General Rule

As a general rule, Place of Supply of services treated as international transactions shall be the location of recipient of service.

Example

A consultant provides service to his U.S. counterpart, this being an international transaction, where the recipient of service is outside India, section 13 comes into focus, under which the place of supply shall be U.S.

B. Non- availability of the location of service recipient

Where the location of service recipient is not available, the place of supply shall be location of the supplier of services.

Example

Consultant provides service to a person outside India, whose location is not known, then the place of service shall be India being the location of the supplier of services

C. Services involving actual performance

Services involving actual performance, place of actual performance of services will be location of service.

Example

An Indian singer performs in a concert in Sydney. Place of service shall be Sydney.

D. Processing of goods

When supply of service involves doing some activity on some goods, place of supply is location of goods.

Example

If packing of goods imported is to be done in London, the place of service shall be London for providing packing service.

E. Services related to immovable property

Services related to immovable property, place of supply of services is location of immovable property.

Example

An Engineer in India makes structural plans for a tower in Dubai. The place of service will be Dubai, not India

F. Event based Services

Place of supply with respect to event based services like exhibition, conference, fair etc. shall be place where such events are held.

Example

1. A decorator organises a business fair in Paris, the place of service will be Paris.
2. An American Event manager organises AIFA award ceremony in Mumbai. The place of service shall be Mumbai. The event manager will have to take registration as a non-resident taxable person at least five days advance of the event.

G. Services of Banking companies, transport hiring and intermediaries

In case of banking company, or intermediary services or hiring of means of transport etc. shall be location of the supplier of services.

Example

1. A German company gives buses on rent to an Indian troupe visiting Berlin and charts a plane for returning to Mumbai. Place of service will be the location of supplier in Germany.
2. Bank charges payable to a London bank, the place of service will be London.

H. Transportation of goods

Place of supply in case of transportation shall be place of destination of such goods.

Example

1. A freight of a Truck carrying goods to Nepal, the place of service shall be Nepal.
2. All ocean going ships or air crafts, place of service will be the destination port.

I. Transportation of passengers

In case of transportation of passengers, place where the passenger embarks on the conveyance.

Example

A travel agent carries passengers from Lucknow to Mansrovar in China, the place of service shall be Lucknow.

J. Online data information

Place of supply of services in case of online information and database access, place of recipient of services.

Example

Charges paid to google or Facebook for making available or data information in India, the place of service shall be India.

Although, the syllabus covers sections 10 and 12 only. But in the context of other topics, it is important to determine whether any supply is import of service attracting IGST on import of services or export of services exempted from GST if the place of supply is outside India. Hence, provisions of section 13 are discussed, as the provisions are both overlapping and relevant.

9. SELF- EXAMINATION QUESTIONS

1. What is the meaning of "location of the recipient of service:
2. Explain the term ' location of provider of service '
3. How the place of service is determined for supply of goods?
4. Explain the rules for determining place of supply of services.
5. What determination of place of service is important?
6. What are the types of taxes, How the will be affected by the place of service.



PAYMENTS OF GST

Synopsis

1. Introduction
2. Recording / Maintenance OF Register/Ledgers
3. Interest on Delayed Payment
4. Payment of GST
5. Tax Deduction at Source (TDS)
6. Collection OF tax AT Source (TCS)
7. Unique Identification Number (UIN)
8. Discrepancy
9. Self- Examination Questions

1. INTRODUCTION

This Lesson deals with payment provisions under GST given in section 49 of the CGST Act, 2017 and the Payment of Tax Rules. Main thrust of the provision is on payment of tax, interest, penalty and other amounts payable under the Act through electronic mode “Over the counter payments” have been permitted by cash / cheque/ DD etc. subject to a limit of Rs. 10,000 per challan per tax period. Further, the provisions also provide for maintenance through Electronic Cash Ledger, through Electronic Credit Ledger in the Electronic Liability Register and payment of adjustment of Input Credit of payment through these electronically maintained registers.

2. RECORDING / MAINTENANCE OF REGISTER/LEDGERS :

2.1 Recording and maintenance of register/ledgers on the common portal:-

Following types of Register/Ledgers are maintained on the common portal :

- i. Electronic Liability Register
- ii. Electronic Credit Ledger
- iii. Electronic Cash Ledger.

2.2. Electronic Liability Register

Under section 49(7) of the CGST Act, 2017 read with Rule 1 of Payment of Tax Rules, all liabilities of a taxable person under this Act shall be recorded and maintained in an Electronic Liability Register in Form GST PMT-01. The Register shall contain the debit and credit entries therein as per the following details.

A. Debit Entries

All amounts payable shall be debited to this register, viz. .

- i. Tax and other dues as per return;
- ii. Tax and other dues determined by proper officer;
- iii. Tax & interest due to mismatch;
- iv. Any interest chargeable for delayed payment or late filing of return.

B. Credit Entries

All credits will be made by correspondingly debiting Electronic Cash or Credit Ledger.

C. Sequence of discharging tax and other dues:

Following shall be the chronological order of discharge of tax and other dues

- i. Previous tax period
- ii. Current tax period
- iii. Any other amount payable under this Act.

Illustration:

The Electronic Liabilities Register shows the following liability :

Tax for July ,2018 Rs 25,000 , Assessed Tax for May ,2018 Rs 17,000 and interest for the month of May ,2018 Rs 15,000 , late filing fees Rs 3000 for July 2018. Assuming the tax credit is Rs 40,000 in the month of July, 2018. The liabilities shall be settled as under

Liabilities	Previous tax Period(May)	Current tax period (July)	Any other amount	Total
Balance	17000+ 15,000 = 32,000	25000+3000 = 28,000	NIL	60,000
Credit used	32000	8000	NIL	40,000
Balance	NIL	20,000	NIL	20,000

2.3. Electronic Credit Ledger

Under section 49(2) of the CGST Act, 2017 read with Rule 2 of Payment of Tax Rules, Electronic Credit Ledger shall be to be maintained in Form GST PMT-02 for a registered person and the Ledger shall contain debit and credit entries therein as per the following details:-

A. Credit Entries

- i. Input Tax Credit (ITC) self assessed as per the return as per Section 41 read with Section 49(2) shall be credited to the ledger.
- ii. In case, where the refund is rejected, then ledger shall be re-credited by proper officer by order in Form GST PMT-03.

B. Debit Entries

- i. Utilization of the ITC towards output tax shall be debited to the ledger.
- ii. Unutilized amount in the Electronic Credit Ledger after payment of tax and other dues can be claimed as refund subject to the provisions of Section 54 of CGST Act, 2017 read with Refund Rules and the Ledger shall be debited accordingly.

C. Sequence and restriction for the utilization of Input Tax Credit:-

- i. ITC credit of any tax will be first credited against the liability of that tax only i.e.
 - a. Central tax against central tax,
 - b. State/UT tax against state/UT tax and
 - c. IGST against IGST.
- ii. Ant balance , thereafter of both central and state/UT tax credits can be adjusted against the IGST ;
- iii. IGST credit can be adjusted against central tax and state tax in that order.
- iv. Cross utilization of SGST & CGST & UTGST is not permissible.

In other words :

- a) CGST will be first utilised against CGST, then against IGST.
- b) SGST will be first utilised against SGST, then against IGST.
- c) UTGST will be first utilised against UTGST, then against IGST.
- d) IGST will be first utilised against IGST, then against CGST and thereafter against SGST/UTGST.
- e) Cross utilization of SGST & CGST & UTGST is not permissible

This is given in the following table :

Input Tax Credit	Can be utilized against	Order of utilization	
CGST	CGST & IGST	1. CGST	2. IGST
SGST	SGST & IGST	1. SGST	2. IGST
UTGST	UTGST & IGST	1. UTGST	2. IGST
IGST	IGST, CGST, SGST & UTGST	1. IGST 2. CGST	2. CGST then 3. SGST/UTGST
Cross utilization of SGST & CGST & UTGST is not permissible			

Example –

ITC available – CGST Rs 20,000, SGST Rs. 15,000 IGST Rs 14,000

Outstanding liabilities- CGST 22,000, SGST Rs. 18,000, IGST 10,000

The utilization will be as under :-

Liability	IGST	CGST	SGST
Liabilities balance	14,000	22,000	18,000
Less credits Under same head	10,000	20,000	15,000
Balance Liability / Credit	4,000 (cr)	2,000	3,000
IGST used against CGST , then SGST	4000	2,000	2000
Balance	NIL	NIL	1,000

2.4. Electronic Cash Ledger

2.4.1. Under section 49(1) of the CGST Act, 2017 read with Rule 3 of Payment of Tax Rules, every deposit made towards tax, interest, penalty, fee or any other amount by a person shall be credited to the Electronic Cash Ledger to be maintained in Form GST PMT-05. Following transactions shall have an effect on the Electronic Cash Ledger and shall be debited/ credited accordingly: -

A. Entries credited to the Electronic Cash Ledger

- Self-payment
- Tax Deducted at Source (TDS) U/s 51 in deductee's ledger
- Tax Collection at Source (TCS) u/s 52 – in the ledger of the person from whom the tax was collected
- Refund of balance in the Ledger after paying taxes interest, if rejected, shall be re-credited by proper officer by order in Form GST PMT-03;

(Since amount of refund is debited in the Ledger, hence, for any rejection of claim, the entry will be reversed)

B. Entries debited to the Electronic Cash Ledger

- a. Any tax, interest, penalty, fee or any other amount payable by the registered taxpayer,
 - b. Any amount of refund claimed and granted as per rules, of the balance in Electronic Cash Ledger after payment of tax and other dues,
 - c. Interest on delayed payment
- ii. Levy of TDS, TCS, tax under reverse charge and tax in case of composition, can be made by debiting Electronic Cash Ledger only.

3. INTEREST ON DELAYED PAYMENT

When a registered tax payer does not pay the tax on time, interest is payable on such delayed payment u/s 50 and the interest so payable shall be debited to the Ledger. The rate of interest is as under :-

- a) 18% per annum in case of delayed payment
- b) 24% for excess claim of ITC
- c) 24% for excessive reduction in output tax liability

4. PAYMENT OF GST

4.1. Mode of payment

Payment of GST by the taxpayer can be made by two modes, viz.

- a) Online banking;
 - i. Internet banking
 - ii. Debit card/Credit card
 - iii. National Electronic Funds Transfer (NEFT)
 - iv. Real Time Gross Settlement (RTGS)
- b) Over the counter (OTC)
Permitted up to Rs. 10,000 per Challan per tax period by following modes :
 - i. Cash
 - ii. Cheque
 - iii. Demand Draft or Banker's Cheque

4.2. Payment procedure:

- i. Challan is generated in FORM GST PMT – 06 for the tax, interest, etc. to be deposited and such challan shall remain valid for 15 days.
- ii. Payment by non-registered person (e. g – casual or non- resident taxable person) shall be made by generating a temporary identification number.

4.3. Mandate form in case of NEFT and RTGS:

Where the payment is made by way of NEFT or RTGS mode, the mandate form shall be generated along with the challan on the Common Portal and the same shall be submitted to the bank from where the payment is to be made. The mandate form will be valid for 15 days from the date of generation of challan.

4.4. Challan Identification Number (CIN)

On successful payment, a Challan Identification Number (CIN) will be generated and indicated in the challan. On receipt of CIN from the authorised Bank, the amount paid shall be credited to the Electronic Cash Ledger. In case the CIN is not generated or not communicated, the taxpayer may represent in FORM GST PMT – 07 to bank/electronic gateway.

5. TAX DEDUCTION AT SOURCE (TDS)

5.1. Section 51 of the CGST, Act, 2017, provides for

- deduction of tax at source @ 1% of the value of the supply ;
- excluding GST i.e. CGST/ SGST / UTGST / IGST and cess indicated in the invoice ;
- from the payment made or credited to the supplier of taxable goods or services or both to:-
 - i. a department or establishment of the Central Government or State Government; or
 - ii. local authority; or
 - iii. Governmental agencies; or
 - iv. other persons or category of persons notified by the Government on the recommendations of the Council. and
- Total value of such supply, under a contract exceeds rupees 2,50,000.

5.2. The supplier or the receiver of payment is called the deductee and the person deducting the tax is called “the deductor”.

5.3. Tax is not to be deducted if the location of the supplier and the place of supply is in a State / UT is different from the State /UT of registration of the recipient.

5.4. Procedural provisions

- a) Deductor is required to
 - i. Pay the tax deducted to the Government within 10 days of the end of the month of deduction. E.g. Tax deducted for the month of July, shall be paid on or before 10th August and
 - b) issue a TDS certificate to the deductee mentioning the contract value, rate of deduction, amount deducted and paid to the Government and such other prescribed particulars within five days of crediting the amount so deducted to the Government . For delay beyond 5 days, a late fee of 100 rupees per day will be levied till the certificate is issued , subject to a maximum of 5,000 rupees
- c) Effect of TDS will be that :
 - i. The deductee shall claim credit, in his Electronic Cash Ledger, of the tax deducted and reflected in the return of the deductor furnished u/s 39(3) ; and
 - ii. Correspondingly, no refund to the deductor shall be granted, if the amount deducted has been credited to the Electronic Cash Ledger of the deductee.
- d) In case of failure to pay the tax,
 - i. Interest u/ s 50 (1) in addition to the amount of tax deducted will be payable by the deductor; and
 - ii. Amount of unpaid TDS shall be deemed to be the amount in default u/s 73/74 for issuing show cause notice.
- e) The refund to the deductor or the deductee arising on account of excess or erroneous deduction shall be dealt as per section 54:

6. COLLECTION OF TAX AT SOURCE (TCS)

6.1. Under section 52, an electronic commerce operator, not being an agent is required to collect tax at source at prescribed rate not exceeding 1% of the net value of taxable supplies made by other suppliers through such operator if the consideration with respect to such supplies is to be collected by it.

Net value of taxable supplies” means :

- the aggregate value of taxable supplies of goods or services or both,
- made during any month by all registered persons through the operator,
- reduced by the aggregate value of taxable supplies returned to the suppliers during the said month.
- Supply shall not include the services notified under section 9(5)

Example –

During July 2018 different suppliers sold taxable goods valued at Rs 50 lakh through Amazon, an e-commerce operator, out of which goods worth rupees 10 lakh were returned. Amazon collected payment of 30 lakh rupees and supplier for 10 lakh rupees were using their own payment gateway. Amazon shall collect tax at source @ 1% on 30 lakh or 30,000 rupees from the supplier from the payment received.

Procedural Provisions

1. The operator is required to
 - a) pay the tax deducted to the Government by the next 10th from the end of the month of deduction, and
 - b) furnish a statement, electronically, containing the details of outward supplies of goods or services or both effected through it, including the supplies of goods or services or both returned through it, and the amount collected during a month, in prescribed form and manner by that date.
 - c) furnish an annual statement in prescribed form electronically, containing the details of outward supplies of goods or services or both effected through it, including the supplies of goods or services or both returned through it, and the amount collected during the financial year before the thirty first day of December following the end of such financial year.

Example –

- i. Monthly statement for January, 2018 should be filed by 10 February, 2018.
- ii. Annual statement for F. Y. 2017-18 should be filed before 31 December, 2018.

- iii. The monthly statement filed as above may be rectified for any omission or incorrect particulars therein, other than as a result of scrutiny, audit, inspection or enforcement activity by the tax authorities, subject to payment of interest u/s 50. Time limit for such rectification is
 - the due date for furnishing of statement for the month of September following the end of the financial year, or
 - the actual date of furnishing of the relevant annual statement, whichever is earlier.
2. The supplier of the goods or services or both through the operator shall claim credit, in his Electronic Cash Ledger, of the amount collected and reflected in the statement of the operator furnished.
3. The statement filed by the operator shall be matched with the corresponding details of outward supplies furnished by the concerned supplier.
4. In case of a mismatch between the two statements, the discrepancy shall be communicated to both persons in the prescribed time.
5. If the discrepancy so communicated is not rectified by the supplier in his valid return or the operator in his statement for the month in which discrepancy is communicated, shall be added to the output tax liability of the said supplier, If the value of outward supplies furnished by the operator is more than the value of outward supplies furnished by the supplier, in his return for the month succeeding the month in which the discrepancy is communicated.
6. The concerned supplier, in whose output tax liability any amount has been added shall pay the tax payable in respect of such supply along with interest, u/s 50(1) on the amount so added from the date such tax, was due till the date of its payment.
7. Any authority not below the rank of Deputy Commissioner may serve a notice, either before or during the course of any proceedings under this Act, requiring the operator to furnish such details relating to :
 - (a) supplies of goods or services or both effected through such operator during any period; or
 - (b) stock of goods held by the suppliers making supplies through such operator in the godowns or warehouses, managed by such operator and declared as additional places of business by such suppliers, specified in the notice.
8. Every operator on whom a notice has been served shall furnish the required information within fifteen working days of the date

of service of such notice. Failure will invite a penalty up to 25,000 rupees in addition to any action under section 122.

9. The power to collect the amount shall be without prejudice to any other mode of recovery from the operator.

7. UNIQUE IDENTIFICATION NUMBER (UIN)

A Unique Identification Number (UIN) shall be generated, when any payment is made through electronic cash or credit ledger, or any other amount is debited or credited in the said ledgers. The UIN relating to discharge of any liability shall be indicated in the corresponding entry in the Electronic Liability Register.

8. DISCREPANCY

Any discrepancy in Electronic Liability Register, Electronic Credit or Cash Ledger is required to be communicated to the proper officer in FORM GST PMT-04.

9. SELF- EXAMINATION QUESTIONS

1. List out various forms in connection with payment of GST.
2. What is Electronic Liability Register? Explain the contents of Electronic Credit or Cash Ledger
4. What is rate of interest of delayed payment /
5. What are the provisions regarding TDS.
6. Discuss the responsibility of an e- commerce operator for collection of tax.



COLLECTION OF TAXES UNDER IGST, ACT, 2017

Synopsis

1. Introduction and Objectives
2. Cross-Utilisation of Credit
3. Nature and Place OF Supply
4. Self-Examination Questions

1. INTRODUCTION AND OBJECTIVES

1. Under the pre- GST tax regime, States and Union Territories collected local sales tax or VAT on Intrastate sales of goods within the state /UT. The Central Sales Tax Act, 1956(CST) regulated the interstate trade or commerce. Although, the CST Act is a central law, the levy and collection of taxes on sales of goods in the course of inter-State trade is delegated entirely to the states of origin of goods taking place in the course of interstate trade or commerce.

2. The tax regime suffered from several flaws, namely:-

- (i) The state of origin of goods collected and retained the CST instead of the destination state having jurisdiction over the consumer. This was contrary to the cardinal principle of taxation that incidence of any indirect tax being a consumption tax should be borne by the consumer.
- (ii) Input Tax Credit (ITC) of CST was not allowed to the buyer resulting in cascading of tax (tax on tax) in the supply chain.
- (iii) CST had its own protocol for compliance and different forms required to be filed viz., C Form, E1, E2, F, I, J Forms etc. which increased the compliance cost of the business and impeded the free flow of trade.
- (iv) The CST provided opportunity for “arbitrage” because of the huge difference between tax rates under VAT and CST levied on intrastate sales and interstate sales respectively.

2. The Goods and Services Tax (GST) replaced the multiple taxes levied and collected by the Centre and the States. The GST is one

multistage value added tax levied on the consumption of goods or services or both. Having regard to its federal character, India adopted a “Dual GST” model, enabling the Centre and States /Union Territories to simultaneously levy GST on every supply of goods or services or both which, takes place within a State or Union Territory i.e.:-

(i) CGST Levied and collected under the authority of CGST Act, 2017 passed by the Parliament,

(ii) (SGST) / UTGST levied and collected under the authority of SGST/ UTGST Acts passed by the states or the Union Territories having legislatures

3. In addition, the parliament passed the Integrated Goods and Services Tax (IGST) Act, 2017 to provide a mechanism to-

- a) monitor the interstate trade of goods and services,
- b) maintain the integrity of ITC chain in interstate supplies, and
- c) ensure that the SGST component accrues to the Consumer State.

4. Under the Act, the Central Government levies and collects IGST on all interstate transactions of taxable goods or services, which is broadly equal to CGST rate plus SGST rate. For instance, CGST rate on intrastate sales of goods is say 5%, then SGST rate will also be 5%. Total tax on the product will be 10%. The IGST rate on interstate taxable supply of these goods will be 10%. This may be clear from the following figure:-

IGST Rate on Interstate Sales (10%) (Sales from one state/UT to another state/ UT)	
CGST Rate (5%)	SGST Rate(5%)
(Intrastate sales within same State/UT)	

This lesson will discuss all these aspects with reference to cross utilization of credits of different taxes against one another and other relevant matters.

2. CROSS-UTILISATION OF CREDIT

Input tax credit can be utilised in the following manner :-

1. The supplier will transfer funds to IGST account in the state of origin. The IGST may be paid by utilising the ITC

2. The buyer in the destination state can utilise IGST credit for payment of CGST and SGST by the transfer of funds from IGST account.
3. The amount of ITC on account of IGST is allowed to be utilised towards the payment in the following order , viz:-
 - a. IGST,
 - b. CGST,
 - c. SGST
4. The amount of ITC on account of CGST is allowed to be utilised towards the payment in the following order , viz:-
 - a. CGST,
 - b. IGST
5. The amount of ITC on account of SGST is allowed to be utilised towards the payment in the following order , viz:-
 - a. SGST,
 - b. IGST,
6. Input tax credit of CGST and SGST cannot be cross utilised.
7. Set off of ITC not available to a person under composition scheme.

Following chart summarises the position

SET OFF OF INPUT CREDIT			
Input Credit	UTILISATION OF INPUT CREDIT		
	First utilisation	Second Utilisation	Balance
CGST	CGST	IGST	No
SGST/UTGST	SGST/UTGST	IGST	No
IGST	IGST	CGST,	SGST/UTGST
Input tax credit of CGST and SGST cannot be cross- utilised			

Following illustrations will explain the position ;

Illustration -1

A of Akola sells goods of Rs 10,000 to G of Goa. The CGST /SGST rate is 5%. Each and IGST rate is 10% integrating the CGST and SGST. G sells these goods in Goa for Rs 12,000.

(a) This is a case of interstate supply of goods involving movement of goods between two different states viz. Maharashtra and Goa liable to IGST. Hence, A will have to transfer Rs. 1000 to IGST account. A can transfer this amount by paying cash or by utilising any ITC due to him.

(b) (i) For G, it will be an intrastate supply within the state of Goa. Hence, G is liable for,

- 5% or Rs. 600 towards CGST and
- 5% or Rs. 600 towards Goa SGST.

(ii) G can avail credit of ITC in respect of IGST of Rs. 1000 in the following manner;

- Firstly, Rs. 600 towards the CGST and
- Then balance Rs. 400 towards the Goa SGST.

G will have to transfer the balance of Rs. 200 towards the Goa SGST.

Illustration -2

Following is the summary of GST payable and input credit available to Ashok :

Tax	Output tax Liability	Input Tax Credit (ITC)
	Rupees	
IGST	35,000	18000
CGST	10,000	15000
SGST	10,000	15000

The tax payable will be calculated as follows:

Tax	Output tax Liability	Input Tax Credit			Cash Payment Balance
		IGST	CGST	SGST	
	Rupees				
IGST	35,000	18000	5,000	5000	7000
CGST	10,000	NA	10,000	NA	0
SGST	10,000	NA	NA	10000	0
Total	55000	18000	15000	15000	7000

Illustration -3

Following is the summary of GST payable and input credit available to Ashok :

Tax	Output tax Liability	Input Tax Credit (ITC)
	Rupees	
IGST	15,000	54000
CGST	36,000	12000
SGST	36,000	12000

The tax payable will be calculated as follows:

Tax	Output tax Liability	Input Tax Credit			Cash Payment Balance
		IGST	CGST	SGST	
	Rupees				
IGST	15,000	15000	NIL	NIL	0
CGST	36,000	24000	12,000	NA	0
SGST	36,000	15000	NA	12000	9000
Total	87000	54000	12000	12000	9000

3. NATURE AND PLACE OF SUPPLY

It is very important to determine the nature of supply – whether it is inter-State or intra-state, as the kind of tax to be paid (IGST or CGST+SGST) depends on that.

(i) Inter-State Supply:

Subject to the place of supply provisions, where the location of the supplier and the place of supply are in:

- (a) Two different States;
- (b) Two different Union territories; or
- (c) A State and a Union Territory.

Such supplies shall be treated as the supply of goods or services in the course of inter-State trade or commerce.

Any supply of goods or services in the taxable territory, not being an intra-State supply, shall be deemed to be a supply of

goods or services in the course of inter-State trade or commerce. Supplies to or by SEZs are defined as inter-State supply.

Further, the supply of goods imported into the territory of India till they cross the customs frontiers of India or the supply of services imported into the territory of India shall be treated as supplies in the course of inter-State trade or commerce.

Also, the supplies to international tourists are to be treated as inter-State supplies.

(ii) Intra-State supply:

It has been defined as any supply where the location of the supplier and the place of supply are in the same State or Union Territory.

Intra- State supply

- Supply of goods within the same State or Union Territory.
- Supply of services within the same State or Union Territory
- Supply of goods from one State or Union Territory to another State or Union Territory
- Supply of services from one State or Union Territory to another State or Union Territory
- Import of goods till they cross customs frontier
- Import of services
- Export of goods or services
- Supply of goods/services to/by SEZ
- Supplies to international tourists
- Any other supply in the taxable territory which is not intra-state supply

Thus, the nature of the supply depends on the location of the supplier and the place of supply. Both these terms have been defined in the IGST Act.

9. Location of Supplier

Broadly, it is the registered place of business or the fixed establishment of the supplier from where the supply is made. Sometimes, a service provider has to go to a client's location for providing service. Such place would not be considered as the location of the supplier. It has to be either a regular place of business or a fixed establishment, which is having sufficient degree

of permanence and suitable structure in terms of human and technical resources.

10. Place of supply

(i) Places of supply provisions have been framed for goods and services, keeping in mind the destination/consumption principle. In other words, **the place of supply is based on the place of consumption of goods or services**. As goods are tangible, the determination of their place of supply, based on the consumption principle, is not difficult.

Generally, **the place of delivery of goods becomes the place of supply**.

However, the services being intangible in nature, it is not easy to determine the exact place where services are acquired, enjoyed and consumed. In respect of certain categories of services, the place of supply is determined with reference to a proxy.

(ii) A distinction has been made between

- B2B (Business to Business) and
- B2C (Business to Consumer) transactions,

B2B transactions are wash transactions since the ITC is availed by the registered person (recipient) and no real revenue accrues to the Government.

(iii) Separate provisions for the supply of goods and services have been made for the determination of their place of supply.

Separate provisions for the determination of the place of supply in respect of domestic supplies and cross border supplies have been framed.

A. Place of supply of goods other than import and export [Section-10]

Nature of Supply Place of Supply

.	Nature of supply	Place of supply
1	Where the supply involves the movement of goods, whether by the supplier, recipient or by any other person	the location of the goods at the time at which, the movement of goods terminates for delivery to the recipient

2.	Where the goods are delivered to the recipient or any person on the direction of the third person by way of transfer of title or otherwise, it shall be deemed it shall be deemed that the third person has received the goods.	The principal place of business of such person
3.	Where there is no movement of goods either by supplier or recipient	Location of such goods at the time of delivery to the recipient
4	Where goods are assembled or installed at site	The place where the goods are assembled or installed
5	Where the goods are supplied on-board a conveyance like a vessel, aircraft, train or motor vehicle	The place where such goods are taken on-board the conveyance
6	Where the place of supply of goods cannot be determined in terms of subsections (2), (3), (4) and (5)	It shall be determined in such manner as may be prescribed

B. Place of supply of goods in case of Import & Export
[Section-11]

S.No.	Nature of supply	Place of supply
1	. Import	Location of importer
2	Export	Location outside India

C. Place of supply of services in case of Domestic Supplies
[Section 12]

(Where the location of supplier of services and the location of the recipient of services is in India) (i) In respect of the following 12 categories of services, the place of supply is determined with reference to a proxy. Rest of the services is governed by a default provision.

S. No.	Nature of supply	Place of supply
1	Immovable property related to services, including hotel accommodation	Location at which the immovable property or boat or vessel is located or intended to be located If Located outside India- Location of the recipient
2	Restaurant and catering	Location where the

	services, personal grooming, fitness, beauty treatment and health service	services are actually performed
3.	Training and performance appraisal	B2B: Location of such Registered Person B2C: Location where the services are actually performed
4.	Admission to an event or amusement park	Place where the event is actually held or where the park or the other place is located
5.	Organisation of an event	B2B: Location of such Registered person B2C: Location where the event is actually held If the event is held outside India: Location of the recipient
6	Transportation of goods, including mails	B2B: Location of such Registered Person B2C: Location at which such goods are handed over for their transportation
7.	Passenger transportation	B2B: Location of such Registered Person B2C: Place where the passenger embarks on the conveyance for a continuous journey
8	Services on board a conveyance	Location of the first scheduled point of departure of that conveyance for the journey
9.	Banking and other financial services	Location of the recipient of services on the records of the supplier Location of the supplier of services if the location of the recipient of services is not available
10	Insurance services	B2B: Location of such Registered Person B2C: Location of the recipient of services on the records of the supplier
11	Advertisement services to the Government	The place of supply shall be taken as located in each of

		such States Proportionate value in case of multiple States
12	Telecommunication services involving fixed line, circuits, dish etc.,	The location of such fixed equipment
	Mobile/ Internet post-paid services,	the location of billing address of the recipient
	Sale of pre-paid voucher	the place of sale of such voucher
	In other cases,	The address of the recipient in records.

(ii) For the rest of the services other than those specified above, a default provision has been prescribed as under: Default Rule for the services other than the 12 specified services Description of Supply Place of Supply

S. No.	Nature of supply	Place of supply
1	B2B	Location of such Registered Person
2	B2C	Location of the recipient where the address on record exists, in other cases Location of the supplier of services

D. Place of supply of services in case of cross-border supplies: (Section 13)

(Where the location of the supplier of services or the location of the recipient of services is outside India)

(i) In respect of the following categories of services, the place of supply is determined with reference to a proxy.

Rests of the services are governed by a default provision.

S. No.	Nature of supply	Place of supply
1	Services supplied for goods that are required to be made physically available from a remote location by way of electronic means (Not applicable in case	The location where the services are actually performed, The location where the goods are situated

	of goods that are temporarily imported into India for repairs and exported)	
2	Services supplied to an individual and requiring the physical presence of the receiver	The location where the services are actually performed
3	Immovable property-related services, including hotel accommodation	Location at which the immovable property is located
4	Admission to or organisation of an event	The place where the event is actually held
5	If the ABOVE services are supplied at more than one locations. i.e., (i) Goods & individual related (ii) Immovable property-related (iii) Event related	
I	At more than one location, including a location in the taxable territory	the location in the taxable territory where the greatest proportion of the service is provided
II	In more than one State	each such State in proportion to the value of services provided in each State
6.	Banking, financial institutions, NBFC Intermediary services, hiring of vehicles' services etc.	Location of the supplier of service
7,	Transportation of goods	The place of destination of the goods
8.	Passenger transportation	Place where the passenger embarks on the conveyance for a continuous journey
9.	Services on-board a conveyance	The first scheduled point of departure of that conveyance for the journey
10.	Online information and database access or retrieval services	The location of recipient of service
11.	Default Rule for the cross border supply of services other than THE ABOVE nine specified services	Any Location of the recipient of service If not available in the ordinary course of business: The location of the supplier of service
12.	Supplies in territorial	Where the location of the supplier

	waters	is in the territorial waters, the location of such supplier, or where the place of supply is in the territorial waters, the place of supply is deemed to be in the coastal State or Union Territory where the nearest point of the appropriate baseline is located.
13	Export/Import of Service	A supply would be treated as import or export, if certain conditions are satisfied. These conditions are as under
	Export	Export of services Means the supply of any service, where a) the supplier of service is located in India, (b) the recipient of service is located outside India, (c) the place of supply of service is outside India, (d) the payment for such service has been received by the supplier of service in convertible foreign exchange, and (e) the supplier of service and the recipient of service are not merely establishments of a distinct person in accordance with explanation 1 of section 8
	Import	Import of services means the supply of any service, where (a) the supplier of service is located outside India, (b) the recipient of service is located in India, and (c) the place of supply of service is in India
13	Zero rated supply	Exports and supplies to SEZs are considered as 'zero rated supply' on which no tax is payable. However, ITC is allowed, subject to such conditions, safeguards and procedure as may be prescribed, and refunds in respect of such supplies may be claimed by following either of these options: (i) Supply made without the payment of IGST under Bond and claim refund of unutilised ITC or

		(ii) Supply made on payment of IGST and claim refund of the same
14.	Refund of integrated tax paid on supply of goods to tourist leaving India - Section 15 of the IGST Act	Refund of IGST paid to an international tourist leaving India on goods being taken outside India, subject to such conditions and safeguards as may be prescribed. An international tourist has been defined as a non-resident of India who enters India for a stay of less than 6 months. IGST would be charged on such supplies as the same in the course of export.

4. SELF-EXAMINATION QUESTIONS

1. Collection of IGST is part of the GST regime, explain?
2. What are rules of cross utilization of credit of one tax against another.
3. How the nature of supply and place of supply affect collection of taxes.
4. What are the limitations of cross- utilization of taxes?

