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1. BASIC CONCEPTS IN INCOME TAX

INTRODUCTION:

- ❖ Tax is the compulsory levy by the government on income, commodity, services, activities or transaction.
- ❖ The word 'tax' derived from the Latin word 'Taxo'.
- ❖ Taxes are the basic source of revenue for the government, which are utilized for the welfare of the people of the country through government policies, provisions and practices.
- ❖ Income Tax is levied on the total income of the previous year of every person, subject to residential status of that person.
- ❖ Further, few of the income of the person are not subject to income tax, those income are termed as exempted income
- ❖ Income Tax in India is governed by Income Tax Act 1961 which came into force from 01.04.1962.
- ❖ The administration of Direct Taxes is with Central Board of Direct Taxes (CBDT).
- ❖ The Act also empowers CBDT to issue circulars, notifications from time to time.
- ❖ A person may generate income from various sources. However, for the purpose of taxation, he is required to classify his income from various sources into 5 heads of income. Each head of income has separate code for computing income under respective head. Thus, classification of income into different heads of income is required to be done carefully
- ❖ All income of a person shall be classified under the following five heads:
 1. Salaries;
 2. Income from house property;
 3. Profits and gains of business or profession;
 4. Capital gains;
 5. Income from other sources

COMPONENTS OF INCOME TAX LAW

The Central Government has got the power through Entry 82 of the Union List of Schedule VII of the Constitution of India to impose tax on all incomes, except the agricultural income. Entry 46 of the State List of said Schedule VII gives power to the State Government to impose tax on agricultural income.

The various components of Income-tax Law, as framed by the Central Government, are -



(1) The Income Tax Act, 1961:

- (a) Charge of income-tax is governed by the Income-tax Act, 1961 which came into force w.e.f. 1 April 1962.
- (b) It extends to whole of India including the state of Jammu & Kashmir.
- (c) It contains the various provisions for determining taxable income, tax liability, procedure for assessment, appeals, penalties and prosecutions.
- (d) It contains 298 Sections and XIV Schedules.



(2) The income Tax Rules, 1962:

- (a) Section 295 of the Act empowers the Central Board of Direct Taxes (CBDT) to make Rules.
- (b) These Rules are notified by Notification in the Official Gazette.
- (c) **Prescribed:** Wherever in the Act the phrase 'as prescribed' appears, it means that Rules have been framed in this respect.



(3) Circulars & Notifications:

- (a) Section 119 of the Act empowers the CBDT to issue orders, instructions and directions for the proper administration of the Act.
- (b) The Income tax Authorities are bound by these particulars.
- (c) They are not binding on assessee, Income Tax Appellate Tribunal (ITAT) or the Courts. However, the assessee can claim benefit under such circulars.

(4) Judicial Decisions:

- (a) Supreme Court's precedent is binding on all the Courts, Appellate Tribunals, Income tax authorities, and on all assessees. Where any two judgments of Supreme Court are contradictory then the decision of the larger bench whether earlier or later in time shall prevail. However, where benches having equal number of judges give contradictory decisions, then, the later decision shall prevail.
- (b) High Court's precedents are binding on the Tribunal, Income tax authorities and on assessees falling under its jurisdiction.



(5) Annual Finance Act:

- (a) **Presenting the Finance Bill:** Every year, the Finance Minister of India presents a Finance Bill in the Parliament, which contains various amendments proposed to be made in the direct and indirect taxes levied by the Central Government.

(b) Approval and assent of Bill: As soon as the Bill is passed by both the houses of the Parliament and thereafter receives the assent of the President of India, it becomes the Finance Act.

(c) Incorporation of Amendments: The amendments proposed therein are then incorporated in the Income Tax Act which are applicable from the very first day of the next financial year.

Example: Generally, amendments by Finance Act, 2021 are effective from 1-4-2022.

(d) First schedule to Annual Finance Act: It contains four parts, which, as applicable for the Finance Act, 2021, are as follows —

| | |
|-----------------|--|
| Part I | It specifies the rates at which income tax is to be levied on income chargeable to tax for the assessment year 2021-22. |
| Part II | It lays down the rate at which tax is to be deducted at source during the financial year 2022-23 i.e. assessment year 2023-24. |
| Part III | It lays down the rates for charging income-tax in certain cases, rates for deducting income-tax from income chargeable under the head Salaries' and the rates for computing advance-tax for the financial year 2022-23 i.e. assessment year 2023-24. |
| Part IV | It lays down the rules for computation of net agricultural income. |

CONCEPT OF CHANGE OF INCOME TAX, PERSON,

ASSESSEE, AND EXCEPTIONS TO PREVIOUS YEAR RULE

Charge of income-tax [Section 4]:

- i) Income tax is charged for every assessment year.
- ii) It is charged on every person as specified under section 2(31) of the Act.
- iii) It is charged on the total income earned by the person during the previous year.
- iv) Total income is computed in accordance with the provisions of the Act.
- v) The tax is levied at the rates prescribed by the Finance Act.
- vi) Income-tax shall be deducted at source or paid in advance, where it is so deductible or payable under any provision of the Act.
- vii) Income Tax Act, as amended on 1st April of any financial year shall apply for assessment of that year.



Example: The law amended on 1-4-2023 shall be applicable for assessment year 2023-24.

Scope of "Person" in accordance with the Act.

The scope of person is explained as under -

(1) Person [Section 2(31)] : "Person" includes,—

- (a) Individual (natural persons, minors and persons of unsound mind).
- (b) Hindu Undivided Family (HUF).
- (c) Partnership firm (including a "Limited Liability Partnership" firm).
- (d) Company.
- (e) Association of persons (AOP) or Body of Individuals (BoI), whether incorporated or not.
- (f) Local authority.
- (g) Every artificial juridical person not falling in any of the above categories. Example: Deities, Idols, Corporation, Bar council, Guru Granth Sahib, Universities etc.

(2) Profit motive not essential to constitute person [Explanation]: An association of persons or a body of individuals or a local authority or an artificial judicial person shall be deemed to be a person, whether or not such person or body or authority or judicial person was formed or established or incorporated with the object of deriving income, profits or gains.

Assessee:-

Assessee [Section 2(7)]: "Assessee" means any person by whom any tax or any other sum of money is payable under this Act and includes —

- (1)** Every person in respect of whom any proceedings under this Act has been taken -
 - (a)** for the assessment of his income or of the income of any other person in respect of which he is assessable; or
 - (b)** to determine the loss sustained by him or by such other person; or
 - (c)** the amount of refund due to him or to such other person;
- (2)** Every person who is deemed to be an assessee under any provision of this Act.

Example: A trustee of a trust is a representative assessee and is deemed to be an assessee.

- (3) Assessee in Default:** Every person who is deemed to be an assessee in default under any provision of this Act i.e. an assessee who has failed to comply with any of the duties imposed upon him by the Income-tax Act.

Example: As per Section 140A(3), if an assessee fails to pay the self-assessment tax in accordance with Section 140(1), then he shall be considered as 'assessee in default'.

"Assessment Year".

Assessment Year (Section 2(9)) "Assessment year" means the period of 12 months beginning with the 1st day of April and ending on 31 March of the next year. Income earned in previous year is taxed in the assessment year.

Example: The assessment year 2023-24 is a period of 12 months starting from the 1 April 2023 and ending on the 31st March 2024.

"Previous Year".

Ans: Previous Year [Section 3]: As per Section 2(34) read with Section 3 of the Act, the term "Previous year" means the financial year immediately preceding the assessment year.

Example: For the assessment year 2023-24, the previous year shall be the period from 1 April, 2022 to 31st March, 2023 and the total income of an assessee earned in the previous year 2022-23 is assessed in the assessment year 2023-24.

Previous year in case of newly set-up business or profession?

In case, a business or profession is newly set-up, the previous year shall commence from the date of setting up of the business or profession and end with the said financial year.

Previous year in case where a new source of income comes into existence?

Ans: In case, where a new source of income comes into existence, the previous year shall commence from the date on which the said source comes into existence and end with the said financial year.

Question: 1- Ascertainment of previous year: Ascertain the previous year in the following situations -

- (a)** Mr. X setup his new business on 27-08-2022.

(b) Mr. 'Y's new source of income came into existence on 25-02-2023.

Solution:

(a) The previous year for Mr. X shall be 27-08-2022 to 31-03-2023.

(b) The previous year for Mr. Y shall be 25-02-2023 to 31-03-2023.

Previous year in case of undisclosed sources of income?

Ans: The following undisclosed incomes shall be deemed to be the income of the F.Y. in which they are found.



- (1) **Unexplained Cash Credits [Section 68]:** Where the assessee offers no explanation to the Assessing officer for any sum credited in the books of accounts or the explanation so offered is not satisfactory, then the sum shall be charged as income in the previous year in which it is credited in the books of accounts.
- (2) **Unexplained investments [Section 69]:** Where the assessee fails to record the investments made by him and thereafter offers no explanation or the explanation so offered is not satisfactory, then the value of such investments are taxed as income in the financial year in which such investment is made.
- (3) **Unexplained Money [Section 69A]:** Where the assessee owns any money, bullion, jewellery, etc. and does not record the same in his books of accounts, then the same shall be regarded as his income of the financial year in which it is found, if the assessee fails to offer any explanation regarding such money or the explanation offered by him seems to be unsatisfactory to the Assessing Officer.
- (4) **Investment not fully disclosed [Section 69B]:** In case, it is found that the real value of any investments, money, bullion, etc. is more than the amount recorded in the books and no explanation is offered by the assessee or the explanation so offered is not satisfactory, then such excess amount shall be treated as his income in the financial year in which such investment, etc. is made.
- (5) **Unexplained Expenditure [Section 69C]:** When the assessee incurs any expenditure for which he offers no explanation about its source or offers an explanation which is not satisfactory, then the same shall be considered as his income in the financial year in which such expenditure is incurred.
- (6) **Amount borrowed or repaid on hundi [Section 69D]:** if any amount is borrowed or repaid on hundi through any mode other than the account-payee cheque, then the same shall be regarded as the income in the financial year in which such amount is so borrowed or repaid.

Thus, the taxability of such undisclosed income shall be -

| Section' | Title | Year of taxability |
|----------|------------------------------------|--|
| 68 | Unexplained Cash Credit | Previous year in which credited in the books of account. |
| 69 | Unexplained investment | Financial year in which investment is made. |
| 69A | Unexplained Money | Financial year in which found. |
| 69B | Investment partly disclosed | Financial year in which investment is made. |
| 69C | Unexplained Expenditure | Financial year in which such expenditure is incurred. |
| 69D | Amount borrowed or repaid on hundi | Financial year of borrowing or repayment. |

Exceptions in case of previous year Rule

As per Section 4 of the Income-tax Act, the income earned in a year is taxable in the next year. This is known as Previous Year Rule. However, there are certain exceptions in which income earned in a year is taxable in the same year.

The exceptions to the above rule are as follows -

(1) Shipping business by Non-residents [Section 172]:

(a) This section applies to a non-resident engaged in shipping business and deriving income therefrom by carrying passengers, livestock, mail or goods from a port in India.



(b) 7.5% of the freight paid or payable to the owner or charterer or any person on his behalf, whether in or outside India, shall be deemed to be his total income and shall be taxed at the rate applicable for foreign company i.e. @ 40% (plus surcharge and Health and Education cess). Such tax shall be paid before the departure of the vessel. Thus, income is taxable in the same year in which carriage is collected and not in the immediately following assessment year.

(2) Persons leaving India [Section 174]:

(a) This section applies when it appears to Assessing Officer that an individual may leave India during the current assessment year or shortly after its expiry and he has no intention of returning back to India.

(b) In case of such person, the total income from 1st April of that assessment year up to the probable date of his departure from India shall be taxable in that year itself at the rates applicable to that assessment year.



(3) Association of persons! Body of Individuals or artificial juridical person formed for a particular event or purpose [Section 174A]:

(a) This section applies where the Assessing Officer is of the opinion that any association of persons or body of individuals or an artificial juridical person, formed for a particular event or purpose, may be dissolved in the assessment year in which it is formed or shortly thereafter.

(b) The total income from 1st April of that assessment year up to the date of its dissolution shall be chargeable to tax in that assessment year itself at the rates applicable to that assessment year.

(4) Persons likely to transfer property to avoid tax [Section 175]:

(a) It applies when it appears to the Assessing Officer that a person is likely to charge, sell, transfer, and dispose of or otherwise part with any of his assets so as to avoid his tax liability.



(b) The total income from 1st April of that assessment year to the date when the Assessing Officer commences proceedings under this section shall be chargeable to tax in that assessment year itself at the rates applicable to that assessment year.

(5) Discontinued business [Section 176]

(a) This section applies where any business or profession is discontinued in any assessment year.

(b) The total income from 1st April of that assessment year upto the date of



discontinuance shall be taxable in the year of discontinuance at the discretion of Assessing Officer.

Note: In above 4 cases it is mandatory for the Assessing Officer to assess the income in the year in which it is earned. However, in 5th case it is at discretion of the Assessing Officer to assess the income in the year in which it is earned or in the next year.

CONCEPTS OF INCOME, METHOD OF ACCOUNTING

Income [Section 2(24)]: According to Section 2(24), "Income" includes,-

1. Profits and gains.
2. Dividend.
3. Voluntary contributions received by a trust created wholly or partly for charitable or religious purposes or by an institution established wholly or partly for such purposes or by a scientific research association or games association referred under section 10(21) or by any other notified fund or institution established for charitable or religious purposes referred under section 10(23), or, by any university or other educational institution or hospital or other medical institution referred under section 10(23C), other than those wholly or substantially financed by the Government, or, by an electoral trust approved by the Board in this behalf.
4. The value of any perquisite or profit in lieu of salary taxable under section 17.
5. Any special allowance or benefit, other than the perquisite included under above clause, specifically granted to the assessee to meet expenses wholly, necessarily and exclusively for the performance of duties of an office or employment of profit.
6. 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
7. 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.
8. The value of any benefit or perquisite, whether convertible into money or not, obtained by any representative assessee or by any person on whose behalf or for whose benefit any income is receivable by the representative assessee (referred as '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.
9. Compensation for termination or modification of terms or conditions of agency or management.
10. Income of trade, professional or similar association from specific services to its members.
11. Deemed profits under Section 41 or under Section 59.
12. Profits on sale of an import license as referred under section 28(iia).
13. Cash assistance received or receivable by any person against exports under any scheme of the Government of India, as referred under section 28(iib).

14. Any duty of customs or excise repaid or repayable as drawback, as referred under section 28(iiiic).
15. Value of any benefit or perquisite, whether convertible into money or not, arising from business or exercise of profession, as referred under section 28(iv).
16. Any interest, salary, bonus, commission or remuneration, by whatever name called, due to, or received by, a partner of a firm from such firm.
17. Any capital gains chargeable under section 45.
18. 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.
19. The profits and gains of any business of banking (including providing credit facilities) carried on by a co-operative society with its members.
20. 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.

Explanation:

- (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.
21. Any sum received by the assessee from his employees as contributions to any provident fund or super-annuation fund or any fund set up under the Employees State Insurance Act, 1948 or any other fund for the welfare of such employees.
 22. Any sum received under a Keyman insurance policy including the sum allocated by way of bonus on such policy.
 23. Any sum received on account of non-competing fees and exclusivity rights as covered under section 28(va).
 24. The fair market value of inventory referred to in Section 28(via) [i.e. Fair market value of inventory which is converted into, or treated as a capital asset.]
 25. Any sum of money/immovable property/any property other than immovable property received by an individual/ HUF, the value of which exceeds fifty thousand rupees as referred under section 56(2)(vii).
 26. Shares of a company (not being a company in which the public is substantially interested) received by a private company or a firm either without or at less consideration, as referred under section 56(2)(viii).
 27. Any consideration for issue of shares as exceeds the fair market value of the shares received by a company (not being a company in which the public is substantially interested) as referred to in Section 56(2)(viib).
 28. Any sum of money received as advance, if such sum is forfeited consequent to failure of negotiation for transfer of a capital asset [Section 56(2) (ix)].
 29. Any sum of money or value of property received without consideration or for inadequate consideration by any person [Section 56(2)(x)].

30. Any compensation or other payment referred to in Section 56(2)(xi) [i.e. Any compensation or other payment, due to or received by any person, in connection with termination of his employment or the modification of the term and conditions relating thereto.]

31. Assistance in the form of a subsidy or grant or cash incentive or duty drawback or waiver or concession or reimbursement (by whatever name called) by the Central Government or a State Government or any authority or body or agency in cash or kind to the assessee other than, —

(a) the subsidy or grant or reimbursement which is taken into account for determination of the actual cost of the asset in accordance with the provisions of Explanation 10 to Section 43(1); 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, as the case may be.

Concept of “Income”.

(i) Income means a periodic monetary return which accrues or is expected to accrue regularly from definite and identifiable sources.

(ii) Income normally refers to revenue receipts and it means net receipts, not gross receipts.

(iii) It is taxable either on receipt or due basis.

(iv) Income may be received in cash or in kind. In case, it is received in kind, the valuation shall be as per the prescribed rules or fair market value.

(v) Illegal incomes are taxable in the same manner as legal income.

(vi) Income must be real and not fictitious.

(vii) It must arise from outside sources.

(viii) The same income cannot be taxed twice unless otherwise provided in law.

(ix) Disputed title to income will not withhold its taxability, it will be taxable in the hands of recipient of income.

Various heads of income

Ans: The relevant provisions are discussed as under -

(1) Heads of Income [Section 14] : According to Section 14 of the Act, all the incomes are categorized in the following five heads —

i) Salaries [Section 15-17];

ii) Income from House Property [Section 22-27];

iii) Profits and Gains of Business or Profession [Section 28-44DB];

iv) Capital Gains [Section 45-55A]; and

v) Income from Other Sources [Section 56-59].

(2) Nature of heads of income: The heads of income are mutually exclusive i.e. an income, which falls under one head cannot be brought to tax under any other head of income. The Income-tax Act contains provisions describing the incomes to be included in each of the heads of income listed above.

Correct classification of income under the proper head is mandatory. Incorrect classification to obtain undue incentives in the law may lead to penalties and prosecution.

Expenditure incurred in relation to income not includible in total income [Section 14A]: As per Section 14A, while computing the total income of an assessee —

- (1) No deduction shall be allowed to the assessee in respect of expenditure incurred in relation to income which does not form the part of the total income under the Act.
- (2) The Assessing Officer shall determine the amount of expenditure incurred in relation to such income, if having regard to the accounts of the assessee, he is not satisfied with the correctness of the claim of the assessee in respect of such expenditure made by the assessee.
- (3) The Assessing Officer has the power to determine the amount of such expenditure even if where an assessee claims that no expenditure has been incurred by him in relation to income which does not form part of the total income under this Act.

Differences between Capital, Receipts and Revenue Receipts.

| | Capital Receipts | Revenue Receipts |
|-----|---|--|
| (1) | Receipts relating to fixed capital are capital receipts. E.g.: Receipt on sale of asset is a capital receipt. | Receipts relating to circulating capital are revenue receipts. E.g.: Receipt on sale of stock-in-trade is a revenue receipt. |
| (2) | Compensation received for extinction of a profit earning source (in whole or in part) is a capital receipt. | Compensation received for loss of profits or earnings is a revenue receipt. |
| (3) | Receipt in substitution of source of income is a capital receipt. E.g.: Compensation for loss of employment is a capital receipt. | A receipt in substitution of income is revenue receipt. |
| (4) | Capital receipts are exempt from tax unless expressly taxable. E.g.: Capital gains | Revenue receipts are taxable unless expressly exempt from tax. E.g.: Income exempt under section 10 to 13A. |
| (5) | Compensation received for relinquishing interest (in whole or in part) in a capital asset is a capital receipt. | Compensation received for relinquishing interest in stock-in-trade of the business is a revenue receipt. |
| (7) | Profits from transactions outside the purview of regular trading activities of the assessee are capital receipts. | Profits from transactions entered into the course of business regularly carried on by the assessee or are incidental to or are associated with business, are revenue receipts. |
| (7) | Subsidy is treated as capital receipt if it is given to set-up a new business or to complete a project or to acquire an asset. | Subsidy is treated as revenue receipt if it is given for an existing business or to meet any specific revenue expenditure or by way of reimbursement of such expenditure. |
| (8) | Profits from sale of shares or securities, which were purchased as an investor, are capital receipts. | Profits from sale of shares, which were acquired in the ordinary course of business as a dealer in shares, are revenue receipts. |

“Keyman Insurance Policy” and its taxability.

- (1) Keyman Insurance Policy:** As per Explanation to Section 10(10D), “Keyman insurance policy” means a life insurance policy taken by a person on the life of another person who is or was the employee of the first mentioned person or is or was connected in any manner whatsoever with the business of the first mentioned person and includes such policy which has been assigned to a person, at any time during the term of the policy, with or without any consideration.
- (2) Sum received including bonus** - is income: According to Section 2(24) of the Act - Sum received under Keyman insurance policy including the sum allocated by way of bonus on such policy, is considered as an income.
- (3) Taxability of sums received:**
 - (a)** If it is taken in name of an employee, then the sum received on its maturity (including the bonus on such policy) is taxable as “profits in lieu of salary” under Section 17(3).
 - (b)** In case the policy matures in the hands of the person carrying on business or profession, then the sum received (including bonus) shall be treated as “Profits and Gains of Business or Profession”.
 - (c)** In case the policy is taken in name of any other person (other than employer or employee), then the sum received on its maturity by such person is chargeable to tax as “Income from other sources”.
 - (d)** In case the policy is assigned to any other person before its maturity, the sum received from such policy shall not be exempt from tax.

MODE OF COMPUTATION OF INCOME AND TAX RATES FOR ASSESSMENT YEAR 2023 - 24

23. What are the steps for computation of total income.

Ans: Income-tax is levied on an assessee’s total income. Such total income has to be computed as per the provisions contained in the Income-tax Act, 1961.

- (1)** Determine Residential Status of the individual assessee as per section 6 and determine scope of his total income as per section 5.
- (2)** Compute Income under each head as per sections 15 to 59. [Incomes exempt under section 10 do not form part of total income.]
- (3)** Clubbing provisions u/s 60 to 65 and undisclosed incomes u/s 68 to 69D are to be taken into account.
- (4)** Allow set off and carry forward of losses as given under sections 70 to 80 and the resultant income shall be the Gross Total Income.
- (5)** From Gross Total Income computed in Step 4 above, allow the deductions under Chapter VI-A.
- (6)** After allowing the deductions in Step 5 above, the resultant figure shall be Total Income. Compute income tax on such total income. There are specific rates of tax in case of long-term capital gains u/s 112 and Section 112A, short- term capital gains in case of securities u/s 111A, winnings from lottery etc. u/s 115BB etc.
- (7)** Allow rebate under section 87A from the amount of income tax calculated in step 6 above at the rate of 100% of such income tax subject to maximum of Rs.12,500 if total income does not exceed Rs.5,00,000.

- (8) Add Surcharge at applicable rates if total income exceeds Rs.50 lakhs. Provide marginal relief if the same is available. Tax plus surcharge is to be increased by Health and Education cess @4%.
- (9) Allow rebate under section 86 read with section 110 in case such individual is a member of an Association of Persons, if applicable, and also allow relief under section 89. The balance shall be the tax liability of such individual for that assessment year.
- (10) From such tax liability deduct TDS, TCS, advance tax and self-assessment tax paid by him. The balance shall be the tax payable by such individual.

Mode of computation of total income of an individual and tax liability thereon.

The mode of computation of total income of an individual and tax liability thereon is as under -

Name of assessee:

| Name of assessee: | |
|--|-------------|
| 1. Income from Salaries [Section 15- 17] | XXXX |
| 2. Incomes from House Property [Section 22- 27] | XXXX |
| 3. Profits and gains of business or Profession [Section 28- 44DB] | XXXX |
| 4. Capital Gains [Section 45- 55A] | XXXX |
| 5. Income from Other Sources [Section 56-59] | XXXX |
| Total [(1) + (2) + (3) + (4) + (5)] | XXXX |
| Add: Income of other persons included in assessee's total income (i.e. Deemed incomes to be aggregated with appropriate heads of income) [Section 60- 69D] | XXXX |
| Less: Adjustment on account of set off or carry forward of losses [Section 70-80] | XXXX |
| Gross Total Income | XXXX |
| Less: Deductions under Sections 80C to 80U | XXXX |
| Total Income[rounded off to Rs.10] | XXXX |
| Computation of tax liability: | |
| Tax on total income | |
| Less: Tax rebate u/s 87A | |
| Balance tax after rebate | XXXX |
| Add: Surcharge | XXXX |
| Tax including Surcharge | |
| Add: Health and Education Cess @ 4% | |
| Tax including HEC | |
| Less: Relief under sections 86, 89, 90, 90A and 91 | |
| Tax | XXXX |
| Less: Pre-paid Taxes | XXXX |
| Tax paid on self assessment | XXXX |
| Tax deducted or collected at source | XXXX |
| Tax paid in advance | XXXX |
| Tax payable/Tax Refundable | XXXX |
| Add: Interests under sections 234A, 234B and 234C, if | XXXX |
| Total amount payable (rounded off to ,nearest Rs.10) | XXXX |

List the general rates of income-tax for individual for Assessment Year 2023-24.

The general rates of income-tax for individual for Assessment Year 2023-24 are as under –

| (i) in case of every individual [other than those covered by (ii) to (iii)] HUF, AOP, BOI, and every artificial juridical person | | (ii) in case of resident individual of age 60 years or more but less than 80 years at any time during the previous year | | (iii) in case of resident individual of age 80 years or more at any time during the previous year | |
|--|------|---|------|---|------|
| Income | Rate | Income | Rate | Income | Rate |
| Upto Rs.2,50,000 | Nil | Upto Rs. 3,00,000 | Nil | Upto Rs.5,00,000 | nil |
| Next Rs.2,50,000 | 5% | Next Rs.2,00,000 | 5% | - | - |
| Next Rs.5,00,000 | 20% | Next 5,00,000 | 20% | Next Rs.5,00,000 | 20% |
| Balance | 30% | Balance | 30% | balance | 30% |

(1) Rate of surcharge applicable to individuals/HUF/AOPs/BOIs for assessment year 2023-24:

| | Particulars | Rate of surcharge on income tax | example | |
|-------|---|---------------------------------|---|--|
| | | | Components of total income | Applicable rate of surcharge |
| (i) | Where the total income (including dividend income and income u/s 111A and 112A) exceeds Rs. 50 lakhs but does not exceed Rs.1 crore | 10% | → Dividend Income Rs.5 lakhs; → STCG u/s 111A Rs. 30 lakhs; → LTCG u/s 112A Rs. 25 lakhs; and → Other income Rs.35 lakhs | Surcharge would be levied @ 10% on income-tax computed on total income of Rs. 95 lakhs. |
| (ii) | Where total income (including dividend income and income under section 111A and 112A) exceeds Rs. 1 crore but does not exceed Rs.2 crore | 15% | → Dividend Income 5 lakhs; → STCG u/s 111A Rs.60 lakhs; → LTCG u/s 112A Rs. 65 lakhs; and → Other income Rs.45 lakhs | Surcharge would be levied @ 15% on income-tax computed on total income of Rs.1.75 crores. |
| (iii) | Where total income (excluding dividend income and income u/s 111A and 112A) exceeds Rs.2 crore but does not exceed Rs.5 crore The rate of surcharge on the income tax payable on the portion of dividend income and capital gains chargeable to tax u/s 111A | 25% not exceeding 15% | → Dividend Income Rs. 5 lakhs; → STCG u/s Rs. 54 lakh; → LTCG u/s Rs.112A Rs.55 lakh; and → other income Rs.3 crores | Surcharge would be levied @ 15% on income-tax on: ○ Dividend income of Rs.5 lakhs ○ STCG of Rs.54 lakhs chargeable to tax u/s 111A and ○ LTCG of Rs. 55 lakhs |

| | | | | |
|------|--|------------------------------|---|---|
| | and 112A | | | chargeable to tax u/s 112A ○ Surcharge @25% would be leviable on income tax computed on other income of Rs.3 crores included in total income |
| (iv) | Where total income (excluding dividend income and income u/s 111A AND 112A) exceeds Rs.5 crores The rate of surcharge on the income tax payable on the portion of dividend income and capital gains chargeable to tax u/s 111A and 112A | 37% Not exceeding 15% | → Dividend income Rs. 5 lakhs → STCG U/S 111A Rs.50 LAKHS → LTCG u/s 112A Rs.65 lakhs and → Other income Rs.6 crores | Surcharge @15% is leviable on income tax on: → Dividend income Rs.5 lakhs → STCG of Rs.50 lakhs chargeable to tax u/s 111A and → LTCG of Rs.65 lakhs chargeable to tax u/s 112A Surcharge @37% is leviable on the income tax computed on other income of Rs.6 crores included in total income |
| (v) | Where total income (including dividend income and income u/s 111A and 112A) exceeds Rs.2 crores in cases not covered under (iii) and (iv) above | 15% | → Dividend income 50 lakhs → STCG u/s 111A Rs.60 lakhs → LTCG U/S 112A Rs.55 lakhs and → Other income Rs.1.2 crore | Surcharge would be levied @15% on income tax computed on total income of Rs.2.85 crore. |

Marginal relief:

(a)

- (i) Marginal relief is available in case total income exceeds Rs.50 lakhs. The additional amount of income-tax payable (together with surcharge) on the excess of income over Rs.50 lakhs should not be more than the amount of income exceeding Rs.50 lakhs.

(ii) Where total income exceeds Rs.1 crore, the total amount payable as income-tax and surcharge on such income shall not exceed the total amount payable as income-tax and surcharge on a total income of Rs.1 crores by more than the amount of income that exceeds Rs.1 crores.

(iii) Where total income exceeds Rs2 crore, the total amount payable as income-tax and surcharge on such income shall not exceed the total amount payable as income-tax and surcharge on a total income of Rs2 crores by more than the amount of income that exceeds Rs2 crores.

(iv) Where total income exceeds Rs5 crore, the total amount payable as income-tax and surcharge on such income shall not exceed the total amount payable as income-tax and surcharge on a total income of Rs5 crores by more than the amount of income that exceeds Rs5 crores.

Basic Exemption limit* : The amount of Rs2,50,000 orRs 3,00,000 or Rs5,00,000 is called “maximum amount not chargeable to tax” or “basic exemption limit” applicable to the assessee.

Rebate u/s 87A: In case of resident individual whose total income does not exceed Rs.5,00,000, rebate shall be allowed from Income tax @ 100% of such tax or Rs12,500 whichever is less.

As per section 115BAC, individuals and HUF have an option to pay tax in respect of their total income (other than income chargeable to tax at special rates under Chapter XII) at following concessional rates, if they do not avail certain exemption deductions like Leave Travel Concession, standard deduction under the head “Salaries”, interest on housing loan on self-occupied property, deductions under Chapter VI-A [other than 80CCD(2) and section 80JJAA] etc. -

| Total income | Rate |
|----------------------------------|------|
| Upto Rs. 2,50,000 | 5% |
| From Rs 2,50,001 to Rs5,00,000 | 10% |
| From Rs 50,00,001 to Rs 7,50,000 | 20% |
| From Rs7,50,001 to Rs10,00,000 | 20% |
| From Rs10,00,001 to Rs12,50,000 | 25% |
| From Rs12,50,001 to Rs15,00,000 | 30% |

Individuals and HUF exercising option u/s 115BAC are not liable to alternate minimum tax u/s 115JC.

Clarification regarding attaining prescribed age of 60 years / 80 years on 31 March itself, in case of senior/very senior citizens whose date of birth falls on 1 April [Circular No. 28,2016, dated 27-07-2016]:

- An individual who is resident in India and of the age of 60 years or more (senior citizen) and 80 years or more (very senior citizen) is eligible for a higher basic exemption limit of Rs.3,00,000 and Rs.5,00,000, respectively.
- The CBDT has, vide this Circular, clarified that a person born on 1 April would be considered to have attained a particular age on 31stMarch, the day preceding the anniversary of his birthday. In particular, the question of attainment of age of eligibility for being considered a senior/very senior citizen would be decided on the basis of above criteria.
- Therefore, a resident individual whose 60thbirthday falls on 1stApril, 2022, would be treated as having attained the age of 60 years in the P.Y. 2022-23, and would be eligible for higher basic

exemption limit of Rs.3 lakh in computing his tax liability for AY. 2023-24. Likewise, a resident individual whose 80th birthday falls on 1st April, 2022, would be treated as having attained the age of 80 years in the P.Y. 2022-23, and would be eligible for higher basic exemption limit of Rs.5 lakhs in computing his tax liability for A.Y. 2023-24;

Special rates of Income-tax for the Assessment Year 2023-24.

The various categories of incomes chargeable to tax at the special rates of income-tax are as follows —

| Section | Nature of income | Rate of tax | | | | | | |
|--|---|------------------------------|------------------------|----------------------------|--|--|-------------------------|-----|
| 111A | Short term capital gains and HUF exercising option u/s 115BAC are not liable to alternate minimum tax u/s 115JC. | 15% | | | | | | |
| 112 | Long-term capital gains (other than LTCG taxable as per section 112A) | 20% | | | | | | |
| 112A | <p>Long term capital gains on transfer of -</p> <ul style="list-style-type: none"> ➤ Equity share in a company ➤ Unit of an equity oriented fund ➤ Unit of business trust <p>Condition for availing the benefit of this concessional rate is Securities Transaction tax should have been paid</p> <table border="1" style="width: 100%; border-collapse: collapse;"> <thead> <tr> <th style="width: 50%;">In case of - (Capital Asset)</th> <th style="width: 50%;">Time of payment of STT</th> </tr> </thead> <tbody> <tr> <td>Equity shares in a company</td> <td>company both at the time of acquisition and transfer</td> </tr> <tr> <td>Unit of equity oriented fund or unit of business trust</td> <td>at the time of transfer</td> </tr> </tbody> </table> <p>Note: LTCG upto 1lakh is exempt. LTCG exceeding Rs.1 lakh is taxable @ 10%.</p> | In case of - (Capital Asset) | Time of payment of STT | Equity shares in a company | company both at the time of acquisition and transfer | Unit of equity oriented fund or unit of business trust | at the time of transfer | 10% |
| In case of - (Capital Asset) | Time of payment of STT | | | | | | | |
| Equity shares in a company | company both at the time of acquisition and transfer | | | | | | | |
| Unit of equity oriented fund or unit of business trust | at the time of transfer | | | | | | | |
| 115BB | 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. | 30% | | | | | | |
| 115BBE | Income referred to in section 68 (Unexplained Cash Credits) or section 69 (Unexplained investments) or section 69A (Unexplained Money) or section 69B (Investment not fully disclosed) or section 69C (Unexplained Expenditure) or section 69D (Amount borrowed or repaid on hundi). Tax is to be increased by surcharge @ 25% of such tax and Health and Education cess @ 4% of such tax and surcharge. The effective rate of tax u/s 115BBE would, therefore, be 78% of such undisclosed income etc., if declared in the return of income. In case the same is not shown in the return of income, there would be a further levy of penalty under new section 271AAC @ 10% of Tax payable u/s 115BBE. | 60% | | | | | | |
| 115BBF | Income by way of royalty in respect of a patent developed and registered in India in respect of person who is resident in India. | 10% | | | | | | |
| 115BBG | Income from transfer of carbon credits. | 10% | | | | | | |

Tax rates incase of assessees other than individuals.

(1) In the case of co-operative society

| | |
|----------------|-----|
| Upto Rs.10,000 | 10% |
| Next Rs.10,000 | 20% |
| balance | 30% |

(a) Surcharge on Income-tax: The amount of income-tax computed above, shall be increased by surcharge of 12% if the Total Income exceeds Rs.1 crore.

(b) (ii) Marginal Relief: Marginal relief is available in case total income exceeds Rs.1 crore. The additional amount of income-tax payable (together with surcharge) on the excess of income over Rs.1 crore should not be more than the amount of income exceeding Rs.1 crore.

Note : Co-operative society, resident in India, can opt for concessional rate of tax @ 25.168% [i.e., tax @ 22% plus surcharge @ 10% plus health and education cess (HEC) @ 4%] under section 115BAD in respect of its total income computed without giving effect to deduction u/s 10AA, 32AD, 33AB, 33ABA, 35(1)(ii)/(ia)/(iii), 35(2AA), 35AD, 35CCC, additional depreciation u/s 32(1)(ia), deductions under Chapter VI-A (other than section 80JJAA) etc. and set-off of loss and depreciation brought forward from earlier years relating to the above deductions. The provisions of alternate minimum tax u/s 115JC would not be applicable to co-operative society opting for section115BAD.

In case of Local authority and Partnership firm (including LLP):

| | Local authority | Partnership firm(including limited liability partnership) |
|--|-----------------|---|
| Rate of income tax | 30% | 30% |
| Surcharge on income tax ,if total income exceeds Rs.1crore | 12% | 12% |

Marginal Relief: Marginal relief is available in case total income exceeds Rs. 1 crore. The additional amount of income-tax payable (together with surcharge) on the excess of income over Rs.1 crore should not be more than the amount of income exceeding Rs.1 crore.

In case of domestic company and foreign company:

Domestic Company

| | Domestic Company[Where its total turnover or the gross receipt in the PY 2020-21 does not exceed Rs. 400 crores | Domestic Company | Foreign Company |
|---|---|------------------|-----------------|
| Rate of income tax | 25% | 30% | 40% |
| Surcharge on Income tax, ➤ If total income exceeds 1 crore but does not exceed 10 crores | 7%* | 7%* | 2%* |

| | | | |
|-------------------------------------|-------|-------|------|
| ➤ if total Income exceeds 10 crores | 12%** | 12%** | 5%** |
|-------------------------------------|-------|-------|------|

(i) ***Marginal Relief:** Marginal relief is available in case total income exceeds Rs.1 crore. The additional amount of income-tax payable (together with surcharge) on the excess of income over Rs.1 crore should not be more than the amount of income exceeding Rs.1 crore.

(ii) ****Marginal Relief:** In the case of every company having a total income exceeding Rs.10 crore, the total amount payable as income-tax and surcharge on such income shall not exceed the total amount payable as income-tax and surcharge on a total income of Rs.10 crores by more than the amount of income that exceeds Rs.10 crores.

Question 2—Marginal relief and tax liability - Individual assessee: Compute the tax liability of Mr. X resident individual 40 years of age wherein his total income is Rs.51,00,000 assuming that there is no income in the nature which is chargeable to special rate of tax and he has not opted for the provisions of Section 115BAC of the Act.

Solution: Tax on total income of Rs.51,00,000 (including surcharge @ 10%) = Rs.1476750

Tax on Rs.50,00,000 = Rs.13,12,500

Marginal Relief = Rs.14,76,750 — (Rs.13,12,500 + Rs.1,00,000) = Rs.64,250

Tax liability = (Rs.14,76,750 — Rs.64,250) + 4% of Rs.14,12,500 = Rs.14,69,000

Question :3—Marginal relief and tax liability — Individual assessee: Compute the tax liability of Mr. X a resident individual 40 years of age wherein his total income is 1,00,50,000 assuming that there IS no income in the nature which is chargeable to special rate of tax and he has not opted for the provisions of Section 115BAC of the Act.

Solution: Tax on total income of Rs.1,00,50,000 (including surcharge @ 15%) = Rs.32,51,625

Tax on Rs.1,00,00,000 (including surcharge @ 10%) = Rs.30,93,750

Marginal Relief = Rs.32,51,625 — (Rs.30,93,750 + Rs.50,000) = Rs.1,07,875

Tax liability — (Rs.32,51,625—Rs.1,07,875) + 4% of Rs.3143750= Rs.32,69,000

Question:4 Marginal relief an tax liability — Individual- assessee.: Compute the tax liability of Mr. X a resident individual 40 years of age wherein his total income is 2,00,50,000 assuming that there is no income in the nature which is chargeable to special rate of tax and he has not opted for the provisions section 115BAC of the Act.

Solution: Tax on total income of Rs.2,00,50,000 (including surcharge @ 25%) = Rs.7284375

Tax on Rs.2,00,00,000 (including surcharge @ 15%) Rs.6684375

Marginal Relief = Rs.72,84,375 — (Rs.66,84,375 + Rs.50,000) = Rs.550000

Tax liability = (Rs.72,84,375 - Rs.5,50,000) +4% of Rs.6734375= Rs.7003750

Question:5 Marginal relief and tax liability — Individual assessee , (compute the --tax liability of Mr. X a- resident individual 40 years of age wherein his total income is 5,00,50,000 assuming that there is no income n the nature which is chargeable to special rate of tax and he has not opted for the provisions of Section 115BAC of the Act.

Solution: Tax on total income of Rs.5,00,50,000 (including surcharge @ 37%) = Rs.20,31,3675

Tax on Rs.5,00,00,000 (including surcharge @ 25%) =18,51,5625

Marginal Relief = Rs.2,03,13,675 -- (Rs.1,85,15,625 + Rs.50,000) = Rs.17,48,050

Tax liability = (Rs.2,03,13,675 - Rs.17,48,050) +4% of Rs.18565625 = Rs.19,30,8250

Rebate of income-tax in case of certain individuals [Section 87A]

(1) Eligible Assessee : Resident Individual, whose total income does not exceedRs. 5,00,000.

(2) Amount of Rebate: Lower of —

(a) 100% of Income tax ; or

(b) Rs.12,500.

Note: Rebate under section 87A is, however, not available in respect of tax payable @ 10% on long term capital gains taxable under section 112A.

Rates of various cess?

Ans: In case of every assessee, the amount of tax plus surcharge if any shall be increased by Health and Education Cess(HEC) @ 4% of Income tax and surcharge.

It is leviable to fulfill the commitment of the Government to provide and finance quality health services and universalised quality basic education and secondary and higher education.

Note:

(a) Total income will be rounded off to nearest multiple of Rs.10. (Section 288A)

(b) Tax (including tax deductible at source or advance tax), interest, penalty, fine or any other sum payable, and the refund due under the act shall be rounded off to the nearest multiple of Rs.10. (Section 288B)

Question :6— Tax liability: Compute the tax liability in the following cases if the assessee has not opted for the provisions of Section 115BAC-

| Assessee | Status | Total income (in Rs.) |
|------------------|-------------------------------------|-----------------------|
| 1) Mr. Mohan | Resident Individual of 40 years | 4,90,000 |
| 2) Mrs. Swati | Non-Resident Individual of 65 years | 2,75,000 |
| 3) Mr. Bansal | Resident Individual of 25 years | 5,50,000 |
| 4) Mrs. priyanka | Resident Individual of 21 years | 15,10,000 |
| 5) Mrs. Resham | Resident individual of 60 years | 12,00,000 |
| 6) Mrs. radhika | Resident Individual of 80 years | 18,00,000 |
| 7) Mr. Ganshyam | Resident Individual of 40 years | 50,00,000 |
| 8) Ms. madhuri | Resident Individual of 21 years | 2,50,000 |

Solution: The computation of tax liability is given below -

| Assessee | Total income (Rs.) | Income tax | Rebate u/s87A | income tax after rebate | Hec@4% | Total tax | Total tax (Rounded off) |
|------------------|--------------------|------------|---------------|-------------------------|--------|-----------|-------------------------|
| 1) Mr. Mohan | 4,90,000 | 12,000 | 12,000 | - | - | - | - |
| 2) Mrs. Swati | 2,75,000 | 1250 | - | 1,250 | 50 | 23,400 | 1,300 |
| 3) Mr. Bansal | 5,50,000 | 22,500 | - | 22,500 | 900 | 23,400 | 23,400 |
| 4) Mrs. Priyanka | 15,10,000 | 2,65,500 | - | 2,65,500 | 10,620 | 2,76,120 | 2,76,120 |
| 5) Mrs. Resham | 12,00,000 | 1,70,000 | - | 1,70,000 | 6,800 | 1,76,800 | 1,76,800 |

| | | | | | | | | |
|----|--------------|-----------|-----------|---|-----------|--------|-----------|-----------|
| 6) | Mrs. Radhika | 18,00,000 | 3,40,000 | - | 3,40,000 | 13,600 | 13,65,000 | 3,53,600 |
| 7) | Mr. Ganshyam | 50,00,000 | 13,12,500 | - | 13,12,500 | 52,500 | 13,65,000 | 13,65,000 |
| 8) | Ms. madhuri | 2,50,000 | - | - | - | - | - | - |

Question: 7 - Compute the tax liability in the following cases if the assessee has not opted for the provisions of Section 115BAC-

| Assessee | status | Total income(Rs.) |
|-----------|---------------------------------|-------------------|
| (a) Mr. X | Resident Individual of 40 years | 1,01,00,000 |
| (b) Mr. Y | Resident Individual of 50 years | 1,10,00,000 |
| (c) Mr. Z | Resident Individual of 55 years | 1,00,00,000 |
| (d) Mr. A | Resident Individual of 55 years | 51,00,000 |
| (e) Mr. B | Resident Individual of 55 years | 2,00,00,000 |
| (f) Mr. C | Resident Individual of 25 years | 2,01,00,000 |
| (g) Mr. D | Resident Individual of 30 years | 5,00,00,000 |
| (h) Mr. E | Resident Individual of 40 years | 5,01,00,000 |

Solution: The computation of tax liability is given below -

| Assessee | Total income (Rs.) | Tax | Surcharge@37% / 25%/15%/10% | Tax incl. surcharge | Marginal relief | Balance tax | HEC@4% | Total tax (rounded off) |
|-----------|--------------------|-------------|-----------------------------|---------------------|-----------------|-------------|----------|-------------------------|
| (a) Mr. X | 1,01,00,000 | 28,42,500 | 4,26,375 | 32,68,875 | 75,125 | 31,93,750 | 1,27,750 | 33,21,500 |
| (b) Mr. Y | 1,10,00,000 | 31,12,500 | 4,66,875 | 35,79,375 | - | 35,79,375 | 1,43,175 | 37,22,550 |
| (c) Mr. Z | 1,00,00,000 | 28,12,500 | 2,81,250 | 30,93,750 | - | 30,93,750 | 123,750 | 32,17,500 |
| (d) Mr. A | 51,00,000 | 13,42,500 | 1,34,250 | 14,76,750 | 64,250 | 14,12,500 | 56,500 | 14,69,000 |
| (e) Mr. B | 2,00,00,000 | 58,12,500 | 8,71,875 | 66,84,375 | - | 66,84,375 | 2,67,375 | 69,51,750 |
| (f) Mr. C | 2,10,00,000 | 58,42,500 | 14,60,625 | 73,03,125 | 5,18,750 | 67,84,375 | 2,71,375 | 70,55,750 |
| (g) Mr. D | 5,00,00,000 | 1,48,12,500 | 37,03,125 | 1,85,15,625 | - | 1,85,15,625 | 7,40,625 | 1,92,56,250 |
| (h) Mr. E | 5,01,00,000 | 1,48,42,500 | 54,91,725 | 2,03,34,225 | 17,18,600 | 1,86,15,625 | 7,44,625 | 1,93,60,250 |

THE END

2. RESIDENTIAL STATUS

Taxability of income of a person depends on his chances of utilization of Indian resources. In whose case chances of utilization of Indian resources are high, he will pay tax more and vice versa.

Three different categories of residential status of an individual. The incidence of tax on any assessee depends upon his residential status under the Act. For all purposes of income-tax, taxpayers are classified into three broad categories on the basis of their residential status.

- (1) Resident
- (2) Not ordinarily resident
- (3) Non-resident

Residential status of an individual [Section 6(1)]: An individual is said to be a Resident in India in any previous year if he satisfies one or both of the basic conditions as given under section 6(1).

➤ **Basic conditions:**

- (1) He must be in India for a period of **182 days** or more during the previous year; or
- (2) He must be in India for a period of **60 days** or more during the previous year and 365 days or more during the four years preceding the previous year.

Exceptions: As per Explanation to Section 6(1),

- (1) the period of 60 days [given in (2) above] is substituted by 182 days in case of an individual -
 - (i) being an Indian citizen, leaves India during the previous year for employment outside India;
 - (ii) being an Indian citizen, leaves India during the previous year as a member of the crew of an Indian Ship;
 - (iii) being an Indian citizen or a person of Indian origin, who being outside India, comes on a visit to India in the previous year.
- (2) the period of 60 days [given in (2) above] is substituted by **120 days** in case of an individual being an Indian citizen or a person of Indian origin, who being outside India, comes on a visit to India in the previous year, having total income, other than the income from foreign sources, exceeding **Rs.15** lakh during the previous year.

“Income from foreign sources” means income which accrues or arises outside India (except income derived from a business controlled in or a profession set up in India) and which is not deemed to accrue or arise in India.

- **Person is deemed to be of Indian origin** According to Explanation to Section 115C(e), a person is deemed to be of Indian origin, if he, or either of his parents, or any of his grandparents was born in undivided India.
- **Period of stay in case Indian citizen being crew member of foreign bound ship - To be determined in prescribed manner [Explanation 2]:** In the case of an individual, being a citizen of India and a member of the crew of a foreign bound ship leaving India, the period or periods of stay in India shall, in respect of such voyage, be determined in the manner and subject to such conditions as may be prescribed.

Computation of period of stay in India in certain cases [Rule 126 of Income Tax Rules, 1962]:

- (1) For the purposes of Section 6(1), in case of an individual, being a citizen of India and a member of the crew of a ship, the period or periods of stay in India shall, in respect of an eligible voyage, not include the period computed in accordance with sub-rule (2).

(2) The period referred to in sub-rule (1) shall be the period beginning on the date entered into the **Continuous Discharge Certificate** in respect of joining the ship by the said individual for the **eligible voyage** and ending on the date entered into the Continuous Discharge Certificate in respect of signing off by that individual from the ship in respect of such voyage.

Explanation: For the purposes of this rule,

(a) **“Continuous Discharge Certificate”** shall have the meaning assigned to it in the Merchant Shipping (Continuous Discharge Certificate-cum Seafarer’s Identity Document) Rules, 2001 made under the Merchant Shipping Act, 1958;

(b) **“Eligible voyage”** shall mean a voyage undertaken by a ship engaged in the carriage of passengers or freight in international traffic where

(i) for the voyage having originated from any port in India, has as its destination any port outside India; and

(ii) for the voyage having originated from any port outside India, has as its destination any port in India.

Note:

(a) **As per Section 2(25A), “India”** means the territory of India, its territorial waters, seabed and subsoil underlying such waters, continental shelf, exclusive economic zone or any other maritime zone. The term “stay in India” includes stay in the territorial waters of India (i.e. 12 nautical miles into the sea from the Indian coastline). Even the stay in a ship or boat moored in the territorial waters of India would be sufficient to make the individual resident in India.

(b) The period of stay in India is not compulsorily required to be active or continuous.

(c) It is not necessary for an individual to stay at his usual place of residence, business or employment.

(d) While counting the number of days of stay in India, the day of arrival as well as departure are included for stay in India.

(e) Where an individual is in India for a part of a day, then the total number of hours for which he stayed in India shall be calculated and a total of 24 hours shall be considered equivalent to one day.

(f) The residence has no relation with citizenship, place of birth or domicile, hence a person can be resident in India even if he is not an Indian citizen.

Individual will be deemed to be resident in India.

Deemed Resident in India [Section 6(1A)]: An individual shall be deemed to be resident in India if he fulfills the following conditions:

(1) He must be citizen of India;

(2) His total income, other than the income from foreign sources, must exceed Rs.15 lakh during the previous year; and

(3) He is not **liable to tax** in any other country or territory by reason of his domicile or residence or any other criteria of similar nature.

If these conditions are satisfied he is deemed to be Not Ordinarily resident in India as per section 6(6)(d).

Non Applicability [Explanation]: The above provisions shall not apply in case of an individual who is said to be resident in India in the previous year under Section 6(1).

Income from foreign sources' means income which accrues or arises outside India (except income derived from a business controlled in or a profession set up in India) and which is not deemed to accrue or arise in India].

Liable to tax, in relation to a person and with reference to a country, means that there is an income-tax liability on such person under the law of that country for the time being in force. It also includes a person who has subsequently been exempted from such liability under the law of that country.

Individual regarded as 'Not ordinarily Resident'.

The relevant provision regarding Not ordinarily Resident (NOR) are discussed as under -

- (1) Not Ordinarily Resident:** Only individuals and Hindu undivided family can be 'not ordinarily resident'. (Others are resident or non-resident). The residential status of an individual is considered as 'not ordinarily resident' if it fulfills —
- (a)** at least one of the conditions as specified under section 6(1) i.e. basic conditions and any of the additional conditions as specified under section 6(6)(a).
 - (b)** he is deemed resident under section 6(1A) read with section 6(6)(d).
- (2) Additional conditions u/s 6(6):** A person is said to be "not ordinarily resident" in India in any previous year if such person has been,-
- (a)** a non-resident in India in any **9 years** out of the total 10 years preceding the previous year; or
 - (b)** in India for a period of **729 days** or less during the 7 years preceding the previous year; or
 - (c)** a citizen of India, or a person of Indian origin, having total income, other than the income from foreign sources, exceeding 15 lakh during the previous year, and he comes to India for the purpose of visit to India during the relevant previous year and he has been in India for a period or periods amounting in all to 120 days or more but less than 182 days; or
 - (d)** a citizen of India who is deemed to be resident in India under section 6(1A). [It may be noted that a deemed resident will always be a resident but not ordinarily resident].

"Income from foreign sources" means income which accrues or arises outside India (except income derived from a business controlled in or a profession set up in India) and which is not deemed to accrue or arise in India].

Person be considered as 'Non-resident'.

When an individual does not satisfy any of the basic conditions mentioned under section 6(1), he becomes nonresident. For him additional conditions are irrelevant.

Determination of residential status of HUF, Partnership firm and company

The provisions relating to determination of residential status are as under —

(1) Hindu Undivided Family (HUF):

- (a) Resident HUF [Section 6(2)] :** HUF is resident in India if the control and management of its affairs is situated wholly or partly in India.
- (b) Non-Resident HUF :** HUF is non-resident in India if the control and management of its affairs is situated wholly outside India.
- (c) Not-Ordinarily Resident HUF [Section 6(6)]:** A resident HUF becomes not-ordinarily resident, if karta or manager satisfies one or both of the following additional conditions:
 - He has been non-resident in India **in 9 out** of the 10 years immediately preceding the relevant previous year; or

- He has been in India **for 729 days** or less during the 7 years immediately preceding the previous year.

Meaning of the term “control and management”:

- The expression ‘control and management’ referred to under section 6 refers to the central control and management and not to the carrying on Of day-to-day business by servants, employees or agents.
- The business may be done from outside India and yet its control and management may be wholly within India .Therefore control and management of a business is said to b situated at a place Where the head and brain of the adventure is situated.
- The place of control may be different from the usual place of running the business and sometimes even the registered office of the assessee. This is because the control and management of a business need not necessarily be done from the place of business or from the place of business or from the registered office of the assessee.
- But control and management do imply the functioning of the controlling and directing power at a particular place with some degree of permanence.

(2) Partnership Firm (or AOP or any other person):

- (a) Resident:** Such person is resident in India if the control and management of its affairs is situated wholly or partly in India.
- (b) Non-resident:** Such person is non-resident in India ii the control and management of its affairs is situated wholly outside India.

(3) Company [Section 6(3)] : A company is said to be resident in India in any previous year, if—

- (a)** it is an Indian company; or
- (b)** its **place of effective management**, 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 the business of an entity as a whole, are in substance made.

Question 1:Sam came to India first time during the P.Y. 2022-23. During the previous year, he stayed in India for

- (i) 50 days;
- (ii) 183 days; &
- (iii) 153 days. Determine his residential status for the A.Y. 2023-24.

Solution:

- (i)** Since Sam resides in India only for 50 days during the P.Y. 2022-23, he does not satisfy any of the conditions specified in sec. 6(1). He is, therefore, a non-resident in India for the P.Y. 2022-23.
- (ii)** Since Sam resides in India for 183 days during the previous year 2022-23, he satisfies one of the conditions specified in sec. 6(1). He is, therefore, a resident in India for the P.Y. 2022-23.
- (iii)** Sam resides in India only for 153 days during the previous year 2022-23. Though he resided for more than 60 days during the previous year but in 4 years immediately preceding the previous year (as he came India first time), he did not reside in India. Hence, he does not satisfy any of the conditions specified in sec. 6(1). Thus, he is a non-resident for the P.Y. 2022-23

Question 2: Determination of Residential status: XYZ Inc. is incorporated in Cayman Island. Its key management and commercial decisions are taken in Board meetings -held in Mumbai during financial year 2022-23. Determine its residential status for assessment year 2023-24

Solution: As per section 6(3), A company is said to be resident in India in any previous year, if its place of effective management, in that year, is in India. In this case though the company is incorporated outside India, it will be regarded as resident in India as its place of effective management during the relevant financial year is in India since its key management and commercial decisions are taken in its board meetings held in Mumbai.

Question 3: Miss Pal, an Indian citizen, left India for first time on 1st April, 2022 for joining job in Tokyo. She came to India on 11th Jan, 2023 for only 170 days. Determine her residential status for P.Y. 2022-23.

Solution:

Number of days Miss Pal stayed in India can be calculated as under:

| P.Y. | Apr | May | June | July | Aug | Sep | Oct | Nov | Dec | Jan | Feb | Mar | Total |
|-------|-----|-----|------|------|-----|-----|-----|-----|-----|-----|-----|-----|-------|
| 22-23 | 1 | - | - | - | - | - | - | - | - | 21 | 28 | 31 | 81 |
| 23-24 | 30 | 31 | 29 | - | - | - | - | - | - | - | - | - | 90 |

Since she left India for employment purpose, hence for becoming resident she has to stay in India for at least 182 days. However, she is in India for only 81 days during the previous year, thus she is a non-resident for the P.Y. 2022-23.

Question 4: X came India for first time on July 24, 2018. From July 24, 2018 to December 25, 2019 he was in India. Again, he came to India on August 5, 2022 for employment purpose & left India on November 25, 2022 permanently. Determine his residential status for the previous year 2022-23 assuming -

(a) He is a foreign citizen (b) He is an Indian citizen

Solution:

During the previous year 2022-23, X was in India for 113 days as shown below:

| Year | Apr | May | June | July | Aug | Sep | Oct | Nov | Dec | Jan | Feb | Mar | Total |
|-------|-----|-----|------|------|-----|-----|-----|-----|-----|-----|-----|-----|-------|
| 22-23 | - | - | - | - | 27 | 30 | 31 | 25 | - | - | - | - | 113 |

Further, he was in India for more than 365 days during 4 years immediately preceding the previous year as shown below:

| Year | Apr | May | June | July | Aug | Sep | Oct | Nov | Dec | Jan | Feb | Mar | Total |
|-------|-----|-----|------|------|-----|-----|-----|-----|-----|-----|-----|-----|-------|
| 18-19 | - | - | - | 8 | 31 | 30 | 31 | 30 | 31 | 31 | 28 | 31 | 251 |
| 19-20 | 30 | 31 | 30 | 31 | 31 | 30 | 31 | 30 | 25 | - | - | - | 269 |
| 20-21 | - | - | - | - | - | - | - | - | - | - | - | - | - |
| 21-22 | - | - | - | - | - | - | - | - | - | - | - | - | - |

As he satisfies condition given in sec. 6(1)(c), he is a resident in India.

Further, he was resident during 2 out of 10 years immediately preceding the relevant previous year but he was in India only for 520 days in 7 years immediately preceding the relevant previous year. As he is not satisfying dual conditions of sec. 6(6), he is a resident but not ordinarily resident in India for the previous year 2022-23.

Note: His status shall remain same in both the cases as –

Question 5: X, a foreign citizen, resides in India during the previous year 2022-23 for 83 days. Determine his residential status for previous year 2022-23 assuming his stay in India during the last few previous years are as follows -

| Year | Days | Year | Days | Year | Days | Year | Days |
|---------|----------|---------|----------|---------|----------|---------|----------|
| 2007-08 | 220 days | 2011-12 | 36 days | 2015-16 | 137 days | 2019-20 | 175 days |
| 2008-09 | 15 days | 2012-13 | 115 days | 2016-17 | 265 days | 2020-21 | 15 days |
| 2009-10 | 257 days | 2013-14 | 123 days | 2017-18 | 310 days | 2021-22 | 67 days |
| 2010-11 | 110 days | 2014-15 | 65 days | 2018-19 | 121 days | | |

Solution:

During previous year 2022-23, X was in India for 83 days & during 4 years immediately preceding the previous year, he was in India for 378 days as shown below:

| Year | 2018-19 | 2019-20 | 2020-21 | 2021-22 | Total |
|-----------------------------|---------|---------|---------|---------|-------|
| No. of days stayed in India | 121 | 175 | 15 | 67 | 378 |

Thus, he satisfies one of the conditions specified u/s 6(1) & consequently, he becomes resident in India in the P.Y.

2022-23. Further, to determine whether X is an ordinarily resident or not, he needs to satisfy both conditions laid down u/s 6(6).

| Year | Presence in India (In Days) | Resident or Non resident | Condition satisfied to become a resident |
|-----------|-----------------------------|--------------------------|--|
| 2021-2022 | 67 | Resident | 6(1)(c) |
| 2020-2021 | 15 | Non Resident | None |
| 2019-2020 | 175 | Resident | 6(1)(c) |
| 2018-2019 | 121 | Resident | 6(1)(c) |
| 2017-2018 | 310 | Resident | Both |
| 2016-2017 | 265 | Resident | Both |
| 2015-2016 | 137 | Non Resident | None |
| 2014-2015 | 65 | Resident | 6(1)(c) |
| 2013-2014 | 123 | Resident | 6(1)(c) |
| 2012-2013 | 115 | Resident | 6(1)(c) |

Condition (i) of sec. 6(6) requires that an individual should be resident in India for at least 2 out of 10 years preceding the relevant previous year. X was resident in India for 8 out of 10 years immediately preceding the previous year. Thus, he satisfies this condition.

Condition (ii) of sec. 6(6) requires that an individual should be present in India for at least 730 days during 7 years preceding to relevant previous year. X was in India for 1090 days during 2015-16 to 2021-22. Hence, he satisfies this condition also.

X satisfies condition (ii) of sec. 6(1) as well as both the conditions of sec. 6(6). Thus, he is a resident and ordinarily resident in India for the previous year 2022-23.

Question 6: Determination of Residential status: Lotus Inc., a US company headquartered at New York, not having a permanent establishment in India, has set up a liaison office in Delhi in April, 2022 in compliance with RBI guidelines to look after its day to day business operations in India, spread awareness about the company's products and explore further opportunities. The liaison office takes decisions relating to day to day routine operations and performs support functions that are preparatory and auxiliary in nature. The significant management and commercial decisions are, however, in substance made by the Board of Directors at New York. Determine the residential status of Lotus Inc. for A.Y. 2023-24

Solution: In the case of Lotus Inc., its place of effective management for P.Y. 2022-23 is not in India, since the significant management and commercial decisions are, in substance, made by the Board of Directors outside India in New York.

Lotus Inc. has only a liaison office in India through which it looks after its routine day to day business operations in India. The place where decisions relating to day to day routine operations are taken and support functions that are preparatory or auxiliary in nature are performed are not relevant in determining the place of effective management.

Hence, Lotus Inc., being a foreign company is a non-resident for A.Y. 2023-24, since its place of effective management is outside India in the P.Y. 2022-23.

SCOPE OF TOTAL INCOME

Scope of total income [Section 5]: The tax incidence in case of different residential status is as follows

| Particulars | Tax Incidence | | |
|--|---------------|-----|-----|
| | R | NOR | NR |
| (1) Income received in India by him or on his behalf (whether accrued in India or outside India). | Yes | Yes | Yes |
| (2) Income deemed to be received in India by him or on his behalf (whether accrued in India or outside India). | Yes | Yes | Yes |
| (3) Income accruing or arising in India (whether received in India or outside India). | Yes | Yes | Yes |
| (4) Income deemed to accrue or arise in India (whether received in India or outside India). | Yes | Yes | Yes |
| (5) income which accrues or arises outside India (other than that covered in cases (1) to (4) above) | Yes | No | No |

Exception: Out of the total income, which accrues or arises outside India that part of income shall be taxable in India which is derived from any business controlled in or profession set up in India.

Note:

- **Foreign income not taxable even if included in Balance Sheet [Explanation 1] :** Foreign income accruing or arising outside India shall not be deemed to be received in India merely because of the reason that it is included in the Balance Sheet prepared in India.
- **Income taxed on accrual basis not taxable again on receipt basis [Explanation 2]:** Income once taxed in the previous year on accrual basis shall not be again chargeable to tax on receipt basis.
- **Receipt of income is important:** Only that income will be taxed in India which is received in India, not remitted to India.

For example: Mr. A, a non-resident, receives some income in USA and remits the same to India thereafter. The income so received in India is not taxable here as it is received in USA, not in India and also it does not accrue in India, only remitted to India.

- **If resident for one source of income, then resident for all the other sources [Section 6(5)]:** If a person is assessed as a resident in India for one of his sources of income, then he shall be deemed to be a resident for all of his other sources of income too.
- **Income should specifically relate to previous year:** Only that income shall be taxed in India which pertains to previous year.

| | |
|--|--|
| Circular No. 13 / 2017, dated 11-04-2017 and Circular No.17/2017 dated 26-04-2017 | Clarification regarding liability to income-tax in India of a non-resident seafarer receiving remuneration in NRE (Non-resident External) account maintained with an Indian Bank: Income by way of salary, received by non-resident seafarers, for services rendered outside India on a foreign going ship (with Indian flag or foreign flag) and received into the NRE bank account maintained with an Indian bank shall not be included in the total income. |
|--|--|

Differences between Receipt and Remittance of income.

| | Receipt | Remittance |
|------------|---|--|
| (1) | It refers to the first occasion when an recipient gets money under his control. | It means subsequent transmission of the money to another place after it is received. |
| (2) | Receipt of income is chargeable to tax. | Remittance of income is not chargeable to tax. |
| (3) | If the person bringing the money from outside India acts as agent of the payer, then the income is said to have been received in India. | If the person bringing the money from outside India acts as an agent of the payee, then the income is said to have been received outside India and subsequently remitted to India. |

Income deemed to be received [Section 7].

The following income shall be deemed to be received in India -

- (1)** The annual accretion in the previous year to the balance at the credit of an employee participating in a recognised provident fund to the extent of the following -
 - (a)** Employer’s contribution in excess of 12% of salary; and
 - (b)** Interest credited to the Recognised Provident Fund account in excess of 9.5% p.a.
- (2)** The transferred balance from a Unrecognized Provident Fund to a Recognised Provident Fund, to the extent taxable as provided in Rule 11(4) of part A of the Fourth Schedule, i.e. to the extent of employer’s contribution and interest thereon.
- (3)** The contribution made by the Central Government or any other employer in the previous year, to the account of an employee under a pension scheme referred to in Section 80CCD.
- (4)** Cash Credit, Unexplained investment, Unexplained Money, Investment not fully disclosed, Unexplained Expenditure, Amount borrowed or repaid on Hundi.
- (5)** Tax deducted at source in the hands of payee.
- (6)** Deemed profits chargeable to tax under the Act.

‘Income accruing and ‘income due’

Accrual refers to the right to receive income, whereas **due** refers to the right to enforce the payment of the same. For example: Salary for work done in December will accrue throughout the month, day to day, but will become due on the salary bill being passed on 31st December or 1 January.

Further, the income which has been taxed on accrual basis cannot be assessed again on receipt basis as it will lead to double taxation.

INCOME DEEMED TO ACCRUE OR ARISE IN INDIA

Income deemed to accrue or arise in India [Section 9]: The following incomes shall be deemed to accrue or arise in India -

| Section | Income |
|-----------------------|---|
| <p>9(1)(i)</p> | <p>All income accruing or arising, whether directly or indirectly, through or from</p> <ul style="list-style-type: none"> - any business connection in India; or - any property in India, or - any asset or source of income in India; or - through the transfer of capital asset situated in India.  <p>Meaning of ‘Business Connection’ : A ‘business connection’ involves a relation between a business carried on by a non-resident, which yields profits or gains and some activity in India, which contributes directly or indirectly to the earning of those profits or gains. It predicates an element of continuity between the business of the non-resident and the activity in India. The expression ‘business connection’ postulates a real and intimate relation between trading activity carried on outside India and trading activity within India, the relation between the two contributing to the earning of income by the non-resident in his trading activity. – CIT v. R.D. Aggarwal & Co.[1956]56 ITR 20 (SC)</p> <p>Business connection includes professional connection. - Barendra Prasad Roy v. ITO [1981]129 ITR 295 (SC)</p> <p>Incomes not deemed to accrue or arise in India [Explanation 1]: The following incomes are not deemed to accrue or arise in India —</p> <p>(a) In the case of a business, in respect of which all the operations are not carried out in India: In the case of a business, other than the business having business connection in India on account of significant economic presence, of which all the operations are not carried out in India, the income of the business deemed to accrue or arise in India shall be only such part of income as is reasonably attributable to the operations carried out in India.</p> <p>(b) Purchase of goods in India for export: Income earned by a non-resident engaged in purchase of goods in India for the purpose of export.</p> <p>(c) Collection of news and views in India for transmission out of India: Income earned by a nonresident engaged in the business of running a news agency/publishing newspapers, magazines, journals, from the activities confined to collection of news and views in India for their transmission out of India.</p> |

- (d) Shooting of cinematograph films in India :** Income earned from operations of shooting cinematograph films in India, by a non-resident being
- (i) an individual who is not an Indian citizen;
 - (ii) a firm not having a partner who is either a citizen of India or resident in India; and
 - (iii) a company not having any shareholder who is either citizen of India or resident in India.
- (e) Activities confined to display of rough diamonds in SNZs:** Income earned by a foreign company engaged in the business of mining of diamonds through or from the activities which are confined to the display of uncut and unsorted diamond in any special zone notified by the Central Government in the Official Gazette in this behalf.
- Apportionment of profit where operations not fully carried on in India [Rule 10]:** In case the income from Indian operations cannot be definitely ascertained, the same may be computed by apportionment -
- (i) At such percentage of Indian turnover as determined by the Assessing Officer;
 - (ii) Taxable profits = Total Profits x Receipts accruing/arising in India ÷ Total Receipts of Business; or
 - (iii) In any other manner as considered suitable by Assessing Officer.

- “Business Connection” shall include any business activity carried out through -
- (a) Concluding agent** — he has and habitually exercises in India, an authority to conclude contracts on behalf of the non-resident or habitually concludes contracts or habitually plays the principal role leading to conclusion of contracts by that non-resident and the contracts are -
 - (i) in the name of the non-resident; or
 - (ii) for the transfer of the ownership of, or for the granting of the right to use, property owned by that non-resident or that non-resident has the right to use; or
 - (iii) for the provision of services by the non-resident.
 - (b) Stocking agent** - he has no authority, but maintains in India a stock of goods/merchandise from which he regularly delivers goods! merchandise on behalf of the non-resident; or
 - (c) Indenting agent** - he secures orders in India, mainly/wholly for the non-resident or for that nonresident and other non-residents controlling, controlled by, or subject to the same common control. [Explanation 2 to Section 9(1)(i)]
- Exceptions:**
- (i) Business activity carried out through a broker, general commission agent or any other agent who is having an **independent status** acting in ordinary course of business, is not regarded as a business connection.
 - (ii) As per **Explanation 3** - Where a business is carried on in India through a person specified in (a), (b) and (c) above, only so much of income as is attributable to the operations carried out in India shall be deemed to accrue or arise in India.

Significant economic presence [Explanation 2A to section 9(1)(i)] : Significant economic presence of a non-resident in India shall also constitute business connection in India.

“Significant economic presence” means —

| | Nature of transaction | Condition |
|-----|--|---|
| (a) | in respect of any goods, services or property carried out by a non-resident in India including provision of download of data or software in India, | Aggregate of payments arising from such transaction or transactions during the previous year should exceed 2 crore. |
| (b) | systematic and continuous soliciting of business activities or engaging in interaction with users in India through digital means | The number of users must be at least 3 lakhs. |

Further, the above transactions or activities shall constitute significant economic presence in India, whether or not, —

- (1) the agreement for such transactions or activities is entered in India;
- (2) the non-resident has a residence or place of business in India; or
- (3) the non-resident renders services in India.

However, where a business connection is established by reason of significant economic presence in India, only so much of income as is attributable to the transactions or activities referred to in (a) or (b) above shall be deemed to accrue or arise in India.

Extension of source Rule [Explanation 3A]: The income attributable to the operations carried outside in India, as referred to in Explanation 1, shall include income from—

- (i) such advertisement which targets a customer who resides in India or a customer who accesses the advertisement through internet protocol address located in India;
- (ii) sale of data collected from a person who resides in India or from a person who uses internet protocol address located in India; and
- (iii) sale of goods or services using data collected from a person who resides in India or from a person who uses internet protocol address located in India,

Explanation 4: The expression “through” shall mean and include and shall be deemed to have always meant and included “by means of”, “in consequence of” or “by reason of”.

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

Indirect transfer provisions not applicable to FPIs: Nothing contained in this Explanation shall apply to an asset or a capital asset, which is held by a nonresident by way of investment, directly or indirectly, in Category-I foreign portfolio investor under the SEBI (Foreign Portfolio investors) Regulations, 2019, made under the SEBI Act, 1992.

9(1)(ii)

Income which falls under the head “Salaries”, if it is earned in India.

Explanation: Salary shall be regarded as earned in India if it is payable for —

- (a) service rendered in India; or

| | |
|------------------|---|
| | (b) the rest period or leave period which is preceded and succeeded by services rendered in India and forms part of the service contract of employment. |
| 9(1)(iii) | Income chargeable under the head “Salaries” payable by the Government to a citizen of India for service rendered outside India. |
| 9(1)(iv) | A dividend paid by an Indian company outside India. |
| 9(1)(v) | Income by way of interest payable by — (a) the Government; or (b) a person who is resident, except where the interest is payable in respect of any debt incurred, or moneys borrowed and used for the purposes of a business or profession carried on by such person outside India or for the purposes of making or earning any income from any source outside India; or (c) a person who is non-resident, where the interest is payable in respect of any debt incurred, or moneys borrowed and used for the purposes of a business or profession carried on by such person in India. |
| 9(1)(vi) | Income by way of royalty payable by - (a) the Government; or (b) a person who is resident, except where the royalty is payable in respect of any right, property or information used or services utilised for the purposes of a business or profession carried on by such person outside India or for the purposes of making or earning any income from any source outside India; or (c) a person who is non-resident, where the royalty is payable in respect of any right, property or information used or services utilised for the purposes of a business or profession carried on by such person in India or for the purposes of making or earning any income from any source in India. |
| | Royalty [Explanation 2]: ‘Royalty’ means consideration including any lump sum consideration for - (i) Transfer of all or any rights (including granting of a licence) in respect of any patent, invention, model, design, secret formula or process, trademark or similar property; (ii) Use or right to use any industrial, commercial or scientific equipment but not including the amount referred to in section 44BB; (iii) Imparting of any information concerning the working of or the use of a patent, invention, model, design, secret formula or process, trade mark or similar property; (iv) Imparting of any information concerning technical, industrial, commercial or scientific knowledge, experience or skill. (v) Use of any patent, invention, model, design, secret formula or process, trademark or similar property. (vi) Rendering of any service in connection with activities referred in (i) to (v) above. (vii) Transfer of all or any rights (including the granting of a licence) in respect of any copyright, literary, artistic or scientific work including films or videotapes for use in connection with radio broadcasting - |

| | |
|--|--|
| | Exclusions: Any consideration, which would be chargeable as income of recipient under head 'Capital Gains' shall not be treated as royalty. |
| | Consideration for use or right to use of computer software is royalty [Explanation 4]: "The consideration for use or right to use of computer software" is royalty as the transfer of all or any rights in respect of any right, property or information includes and has always included transfer of all or any right for use or right to use a computer software (including granting of a licence) irrespective of the medium through which such right is transferred. |
| | Consideration in respect of any right, property or information is royalty [Explanation 5]: Royalty includes and has always included consideration in respect of any right, property or information, whether or not,- (a) the possession or control of such right, property or information is with the payer; (b) such right, property or information is used directly by the payer; (c) the location of such right, property or information is in India. |
| | Scope of term Process [Explanation 6]: The expression "process" includes and shall be deemed to have always included transmission by satellite (including up-linking, amplification, conversion for down-linking of any signal), cable, optic fiber or by any other similar technology, whether or not such process is secret. |
| 9(1)(vii) | Income by way of fees for technical services payable by — (a) the Government; or (b) a person who is resident, except where the fees are payable in respect of services utilised in a business or profession carried on by such person outside India or for the purposes of making or earning any income from any source outside India; or (c) a person who is non-resident, where the fees are payable in respect of any services utilised in a business or profession carried on by such person in India or for the purposes of making or earning any income from any source in India. |
| | 'Fees for technical services' means any consideration (including any lump sum consideration) for the rendering of any managerial, technical or consultancy services (including the provision of services of technical or other personnel). (Explanation 2] |
| | Exclusions: Consideration for any construction, assembly, mining or like project undertaken by the recipient or consideration which would be income of the recipient chargeable under the head "Salaries", shall not be treated as 'fees for technical services'. |
| 9(1)(viii) | Income arising outside India, being any sum of money referred to in Section 2(24)(xviii) i.e. gift of money, paid on or after 05-07-2019 by a person resident in India to a non-resident, not being a company, or to a foreign company. |
| Income deemed to accrue or arise in India to a non-resident by way of interest, royalty and fee for technical services to be taxed irrespective of territorial nexus [Explanation to Section 9]: The income of a non-resident shall be deemed to accrue or arise in India under section 9(1)(v)/(vi)/(vii) and shall be included in the total income of the non-resident, whether or not, — (i) the non-resident has a residence or place of business or business connection in India; or (ii) the non-resident has rendered services in India. | |

| | |
|--|--|
| Circular no. 4/2015, dated 26-03-2015 | Declaration of dividend by a foreign company: The dividends declared and paid by a foreign company outside India in respect of shares which derive their value substantially from assets situated in India would NOT be deemed to be income accruing or arising in India by virtue of the provisions of Explanation 5 to section 9(1)(i). |
|--|--|

Question 7: Ram provides following details of income, calculate the income which is liable to be taxed in India for the A.Y.2023-24 assuming that – **(V.IMP)**

- (a) He is an ordinarily resident
- (b) He is not an ordinarily resident
- (c) He is a non-resident.

| Particulars | Amount |
|--|----------|
| Salary received in India from a former employer of UK | 1,40,000 |
| Income from tea business in Nepal being controlled from India | 10,000 |
| Interest on company deposit in Canada (1/3rd received in India) | 30,000 |
| Profit from a business in Mumbai controlled from UK | 1,00,000 |
| Profit for the year 2012-13 from a business in Tokyo remitted to India | 2,00,000 |
| Income from a property in India but received in USA | 45,000 |
| Income from a property in London but received in Delhi | 1,50,000 |
| Income from a property in London but received in Canada | 2,50,000 |
| Income from a business in Jambia but controlled from Turkey | 10,000 |

Answer:

Calculation of income liable to be taxed in India of Ram for the A.Y.2023-24

| Particulars | Resident & Ordinarily resident | Resident but not ordinarily resident | Nonresident |
|---|--------------------------------|--------------------------------------|-------------|
| Salary received in India from a former employer of UK | 1,40,000 | 1,40,000 | 1,40,000 |
| Income from tea business in Nepal being controlled from India | 10,000 | 10,000 | Nil |
| Interest on company deposit in Canada - | | | |
| - 1/3rd received in India | 10,000 | 10,000 | 10,000 |
| - 2/3rd received outside India | 20,000 | Nil | Nil |
| Profit from a business in Mumbai controlled from UK | 1,00,000 | 1,00,000 | 1,00,000 |
| Past Profit from a business in Tokyo remitted to India | Nil | Nil | Nil |
| Income from a property in India but received in USA | 45,000 | 45,000 | 45,000 |
| Income from a property in London but received in Delhi | 1,50,000 | 1,50,000 | 1,50,000 |

| | | | |
|---|-----------------|-----------------|-----------------|
| Income from a property in London but received in Canada | 2,50,000 | Nil | Nil |
| Income from a business in Jambia but controlled from Turkey | 10,000 | Nil | Nil |
| Income liable to tax in India | 7,35,000 | 4,55,000 | 4,45,000 |

Question 8: Miss Monica, a foreign national, comes India every year for 90 days since 2007-08.

- a) Determine her residential status for the previous year 2022-23.
b) Will your answer differ, if she comes India for 100 days instead of 90 days every year.

Answer:

- a) Since Miss Monica stayed for 90 days during the previous year 2022-23 and for 360 days (90 days x 4 years) during the 4 years immediately preceding the previous year, hence, she is not satisfying any of the conditions of sec. 6(1). Thus, she is a non-resident for the previous year 2022-23.
b) Since Miss Monica stayed for 100 days during the previous year 2022-23 and for 400 days (100 days X 4 years) during the 4 years immediately preceding the previous year, hence, she is satisfying sec. 6(1)(c). Thus, she is resident for the previous year 2022-23. Further, she resides for only 700 days (100 days x 7 years) during the 7 years immediately preceding the previous year. Hence, she does not satisfy one of the conditions of sec. 6(6). Thus, she is resident but not ordinarily resident for the previous year 2022-23.

Question 9: Mr. Sid, a British national, joined XYZ Co. Ltd. as an engineer in India on 1st May, 2012. On 31st December, 2013, he went to Sri Lanka on deputation. On 1st April, 2018, he came back to India and left for Sri Lanka again on 31st May, 2018. He returned to India and joined his original post on 1st July, 2022. Determine his residential status for the A.Y. 2023-24.

Answer:

| SN | P.Y. | Apr | May | June | July | Aug | Sep | Oct | Nov | Dec | Jan | Feb | Mar | Total |
|----|-------|-----|-----|------|------|-----|-----|-----|-----|-----|-----|-----|-----|-------|
| 0 | 22-23 | - | - | - | 31 | 31 | 30 | 31 | 30 | 31 | 31 | 28 | 31 | 274 |
| 1 | 21-22 | - | - | - | - | - | - | - | - | - | - | - | - | 0 |
| 2 | 20-21 | - | - | - | - | - | - | - | - | - | - | - | - | 0 |
| 3 | 19-20 | - | - | - | - | - | - | - | - | - | - | - | - | 0 |
| 4 | 18-19 | 30 | 31 | - | - | - | - | - | - | - | - | - | - | 61 |
| 5 | 17-18 | - | - | - | - | - | - | - | - | - | - | - | - | 0 |
| 6 | 16-17 | - | - | - | - | - | - | - | - | - | - | - | - | 0 |
| 7 | 15-16 | - | - | - | - | - | - | - | - | - | - | - | - | 0 |
| 8 | 14-15 | - | - | - | - | - | - | - | - | - | - | - | - | 0 |
| 9 | 13-14 | 30 | 31 | 30 | 31 | 31 | 30 | 31 | 30 | 31 | - | - | - | 275 |
| 10 | 12-13 | - | 31 | 30 | 31 | 31 | 30 | 31 | 30 | 31 | 31 | 28 | 31 | 335 |

On the basis of data drawn, residential status of Mr. Sid in last few years can be decided as under:

| Year | Previous Year | Presence in India (In days) | Resident (R) or Non resident (NR) | Condition satisfied to become a resident |
|------|---------------|-----------------------------|-----------------------------------|--|
| 1 | 2021-2022 | 0 | NR | None |

| | | | | |
|----|-----------|--------|----|---------|
| 2 | 2020-2021 | 0 | NR | None |
| 3 | 2019-2020 | 0 | NR | None |
| 4 | 2018-2019 | 61 | NR | None |
| 5 | 2017-2018 | 0 | NR | None |
| 6 | 2016-2017 | 0 | NR | None |
| 7 | 2015-2016 | 0 = 61 | NR | None |
| 8 | 2014-2015 | 0 | NR | None |
| 9 | 2013-2014 | 275 | R | 6(1)(a) |
| 10 | 2012-2013 | 335 | R | 6(1)(a) |

Since assessee resided in India for 274 days in the previous year 2022-23, hence he satisfies sec. 6(1)(a). Therefore, he is resident in India.

Further, since he is resident in India for 2 years out of 10 years preceding the previous year (as shown in above working), but resided in India for less than 730 days out of 7 immediately preceding years, hence he does not satisfy one of the conditions of sec. 6(6), therefore, he is resident but not ordinarily resident.

Conclusion: Resident but not ordinarily resident.

THE END

3. SALARIES

- ❖ Salary is the consideration given to a person for the pains he has bestowed upon another's business" -Stroud's Judicial Dictionary
- ❖ Every payment made by an **employer to his employee** for service rendered would be chargeable to tax as salaries.
- ❖ Before an income can become chargeable under the head 'salaries', it is vital that there should exist between the payer and the payee, the relationship of an employer and an employee.



BASIC CONCEPT OF SALARIES

| Component | Amount | Section |
|---|--------|----------|
| ➤ Taxable salary payments and allowances | xxxx | 15,17(1) |
| ➤ Taxable perquisites | xxxx | 17(2) |
| ➤ Profits in Lieu of salary | xxxx | 17(3) |
| Gross Salary | xxxx | |
| Less: (i) Standard deduction | xxxx | 16(ia) |
| (ii) Deduction for entertainment allowance | xxxx | 16(ii) |
| (iii) Deduction for tax on employment | xxxx | 16(iii) |
| Income under the head 'Salaries' | xxxx | |

The charge under the head "Salaries" presumes the relationship of an employer and employee.

An income earned is chargeable to tax under the head "salaries" **if and only if** there exists an employer-employee relationship between the payer and the payee.

The important features to be considered are —

(1) Contract of service: The employer and employee must enter into a **"Contract of Service"** and not the **"Contract for Service"**.

"Contract of service" bounds the employee to work for the employer whereas in **"contract for service"** the payee is not BOUND but he offers the payer to avail his services and pay the fees as a consideration.

(2) Relationship of master & servant: The relationship between employer and employee must be like master and servant wherein the employer has the direct supervision and control over the work of the employee. Also, the employer gives the instructions to employee and the manner to carry out such instructions.

(3) Not a principal-agent relationship: The employer-employee relationship is not a principal-agent relationship because in case of principal-agent relationship, the agent is free to carry out the instructions given by the principal in his own manner.

(4) Illustrations of employer and employee relationship:

(a) Employee v. Independent professional: Miss Y, an actress, is employed in Chopra Films wherein she gets the monthly salary of 1lakh. She acts in various films and all the producers pay directly to Chopra Films. Here, the remuneration received by Miss Y from Chopra Films constitutes her "Salary".

In case Miss Y does not get monthly remuneration from Chopra Films but receives from different producers, then it does not constitute the 'Income from Salaries' and shall be treated as 'Profits & Gains of Business or Profession'.

(b) Paper-setter / invigilator not an employee: If an individual is working in a school as a teacher and gets the remuneration for the same, then such remuneration shall come in the ambit of 'Salaries'.

However, if he sets any examination paper or acts as an invigilator in any examination and gets the fees for the same, then the fees so received shall not constitute salaries and is taxable under the head 'Income from other sources'.

(c) Salary received by MLAs/ MP's: MLA's and MPs are elected representatives and not the government employees, hence the salary received by them will be taxable under the head 'Income from other sources'. However, if they are assigned any charge of ministry, then the remuneration received by them shall be taxable under the head 'Salaries'.



(d) Remuneration received by Judges: Salary received by judges of court is chargeable to tax as 'Salaries' as their employment is created by the Indian Constitution. - **Justice Deoki Nandan Agarwala v. UOI [1999] 237 ITR 872 (SC)**



(e) Retainership fees received by Advocate General: The retainership fees received by an Advocate-General who gives advices to the Government is not 'Salaries' as the same is done by him in his professional capacity.- **CIT v. Govinda swaminathan (1998) 233 ITR 264 (Mad)**

(f) Pay and allowances to Chief Minister is 'salary': In view of Article 164(5) of the Constitution of India, which provides for payment of salary to the Ministers, the pay and allowances received by the Chief Minister from the State Government is chargeable to tax as 'Income from Salaries'. - **Lalu Prasad v. CIT (2009) 316 ITR 186 (Patna).**

Basis of charge of salaries.

(1) Salaries [Section 15]: The following income shall be chargeable to income tax under the head "Salaries"-

(a) Salary taxable on due basis: Any salary due from an employer or a former employer to an assessee in the previous year, whether paid or not.

(b) Advance salary taxable on receipt basis: 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) Arrears of Salary taxable on receipt basis: 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, salary is taxed on due basis or receipt basis whichever is earlier.

(2) Advance salary not to be taxed again on due basis [Explanation 1]: 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.

(3) Salary received by partner of firm to be taxed under profit and gains of business or profession

[Explanation 2]:

Any salary, bonus, commission or remuneration, by whatever name called, due to, or received by, a partner of a firm from the firm shall not be regarded as “salary” for the purposes of this section.

“Salary”.

According to **Section 17(1)**, Salary includes —

- (1)** Wages;
- (2)** Any annuity or pension;
- (3)** Any gratuity;
- (4)** Any fees, commissions, perquisites or profits in lieu of salary or in addition to any salary or wages;
- (5)** Any advance of salary;
- (6)** Any payment received by an employee in respect of any period of leave not availed of by him;
- (7)** The annual accretion to the balance at the credit of an employee participating in a Recognised Provident Fund to the extent it is chargeable to tax.
- (8)** The aggregate of all sums that are comprised in the transferred balance of an employee participating in a Recognised Provident Fund to the extent it is chargeable to tax;
- (9)** The contribution made by the Central Government or any other employer in the previous year, to the account of an employee under a pension scheme referred to in Section 80CCD.

The concept of ‘Salaries’ is as follows —

- (1)** Commission on a fixed percentage of sales comes in the ambit of salary.
- (2)** For taxing an income under the head ‘Salaries’, it is irrelevant whether the assessee is in part-time employment or full-time employment with his employer.
- (3)** If an employee receives salary from more than one employer during any previous year, then the salary from each employer is taxable under the head “Salaries”.
- (4)** Any deductions made by the employer from the employee’s salary like PF deduction, Tax-deduction at source etc. shall also be included in the salary.
- (5)** Salary is taxed on “due” or “receipt” basis, whichever is earlier; therefore, the date when salary becomes due decides whether it is taxable in the previous year or not.

In some cases, salary becomes due on 15th day of the next month. Therefore, when salary becomes due on 1 day of next month in such a case, salary from March 2021 to February, 2022 shall be taxable for the AY 2022-23.

- (6) Place of accrual of salary:** Income which falls under the head “Salaries”, shall be deemed to accrue or arise in India if it is earned in India. i.e. service rendered in India, “Salaries” payable by the Government to a citizen of India for service rendered outside India shall also be deemed to accrue or arise in India. Allowances and perquisites to Government Employee’s being Indian Citizen for services rendered outside India is exempt from tax.
- (7) Salary received from UNO - Exempt:** Salary, emoluments and pension received from the UNO is exempt from tax under section 2 of the United Nations (Privileges and Immunities) Act, 1947.

Advance Salary v/s Loan or advance against salary:

Advance salary means that the employee receives the salary before it becomes due to him and hence it is taxable on receipt basis in the year in which it is received.

| Loan against salary | Advance against salary |
|---|--|
| It means that the employee takes loan from his employer and agrees to pay the same in specified number of instalments and such instalments may be deducted out of salary of the employee due to him in subsequent months. | It means the employee takes advance against his salary and agrees to get the same adjusted from his salary subsequently. Thus, while advance salary is taxable; loan or advance against salary is not taxable. |

Foregoing of salary v/s Surrender of salary:

| Foregoing of salary | Surrender of salary |
|--|--|
| It means that the employee waives his salary after it becomes due or accrues to him. It is taxable in the hands of employee. | It means that the employee surrenders his salary to the Central Government under section 2 of the Voluntary Surrender of Salaries (Exemption from Taxation) Act, 1961. The salary so surrendered shall be exempt from tax. |

Deductions available to an assessee while computing his income under the head 'Salaries'

- (1) **Standard Deduction [Section 16(ia)]:** A deduction of Rs.50,000 or the amount of the salary, whichever is less.
- (2) **Entertainment allowance [Section 16(ii)]:** Only **Government employees** are entitled to avail deduction on account of entertainment allowance. Entertainment allowance is first included in the gross salary and thereafter deduction is given.
The deduction is allowed to the extent of least of the following —
 - (a) Actual amount received; or
 - (b) Rs. 5,000; or
 - (c) 20% of basic salary (salary exclusive of any allowance, benefit or other perquisite)
- (3) **Employment Tax [Section 16(iii)]:** An assessee is allowed deduction of any sum paid by him on account of a tax on employment within the meaning of Article 276(2). Under the said article employment tax cannot exceed Rs.2,500 per month.

Question 1: Rajesh Kumar, an Indian citizen, is posted in the Indian High commission at London during the previous year 2022-23. His emoluments consist of basic pay of Rs.1,40,000 per month and overseas allowance of Rs. 40,000 per month. Besides, he is entitled to airfare for going from and coming to India and also to free use of Government's car at London. He has no taxable income except salary income stated above. His employer did not deduct tax at source. Rajesh Kumar argues that -

- (i) he is not liable to pay tax on salary earned and received outside India since he is a non-resident during the previous year 2022-23, and
- (ii) even if any tax is due, it is the duty of his employer to deduct tax at source and as such he has no responsibility to pay the tax.

Discuss whether his contention is correct

Will it make any difference if Rajesh Kumar is a Foreign citizen? Give reasons.

Solution:

(i) If Rajesh is an Indian Citizen: The argument of Rajesh Kumar is not correct. Since he is an Indian citizen being government employee his salary income is deemed to accrue or arise in India and is taxable in India. In case if employer does not deduct tax at source, the tax is to be paid directly by employee.

The computation of Taxable Salary is as under **(amounts in Rs):**

| | |
|---|-----------|
| Salary (Rs. 1,40,000 x 12) | 16,80,000 |
| Overseas Allowance (Rs.40,000 x 12) & Perquisites shall be exempt u/s 10(7) | Nil |
| Gross Salary | 16,80,000 |
| Less: Standard deduction u/s 16(ia) | 50,000 |
| Income under the head Salaries | 16,30,000 |

(ii) If Mr. Rajesh is a foreign citizen: In case Rajesh Kumar is foreign citizen, then salary income shall not be deemed to accrue or arise in India, and hence not taxable in India.

TAXABILITY OF ALLOWANCES

House Rent allowance (HRA).

(1) House Rent Allowance [Section 10(13A)]: HRA is an allowance granted to an employee for the payment of rent of his residence. Section 10(13A) provides exemption to the assessee who is in receipt of HRA from his employer.

Least of the following shall be **exempt** —

| S. No. | In other cities | In Mumbai, Delhi, Chennai and Kolkata |
|--------|------------------------------|---------------------------------------|
| 1. | Actual HRA received | Actual HRA received |
| 2. | Rent paid less 10% of salary | Rent paid Less 10% of salary |
| 3. | 40% of salary | 50% of salary |

(2) Exemption not applicable: This exemption shall not apply in a case where -

- (a)** the residential accommodation occupied by the assessee is owned by him; or
- (b)** the assessee has not actually incurred expenditure on payment of rent in respect of the residential accommodation occupied by him.

(3) NOTE

- (a)** Salary = Basic pay + Dearness Allowance (if it enters into retirement benefits) + Percentage-wise fixed commission on turnover.
- (b)** Salary is taken on due basis for the period for which HRA is granted.
- (c)** Computation of exempted HRA depends on— (i) HRA actually received, (ii) Amount of rent paid, (iii) 'Salary' of employee and (iv) Place of situation of rented house.

If there is change in any of the factors during the previous year, the exemption should be worked out on 'monthly basis'.

Question 2: Computation of exempted House rent allowance: Arun, a resident of Meerut, receives Rs.38,000 per annum as basic salary. In addition, he gets Rs.12,000 p.a. as dearness allowance, which does not form part of basic salary, 5% commission on turnover achieved by him (turnover achieved by him during the relevant previous year is Rs. 6,00,000)

and Rs.7,000 per annum as house rent allowance. He however pays Rs. 8,000 per annum as house rent. Determine the quantum of house rent allowance exempt from tax.

Solution HRA exempt to the extent least of the following (amount in Rs)'

| | |
|--|--------------|
| (1) Actual HRA received | 7,000 |
| (2) Rent paid — 10% of salary (Rs.8,000-10% of Rs. 68,000) | 1,200 |
| (3) 40% of the salary (40% of 68,000) | 27,200 |
| Exempted HRA | 1,200 |

Note: Salary Rs.38,000+5% of Rs.6,00,000 = Rs.68,000 for the year.

Question 3: Compute the taxable house rent allowance of Mr. Abhijeet from the following data :

- Basic Salary Rs.5,000 p.m., D.A. Rs.2,000 p.m., HRA Rs.4,000 p.m., Rent paid Rs.4,000 p.m. in Pune.
- On 1/07/2022, there is an increment in Basic salary by Rs.1,000.
- On 1/10/2022, employee hired a new flat in Kolkata at the same rent as he was posted to Kolkata.
- On 1/01/2023, employee purchased his own flat and resides there.

Solution :

Computation of taxable house rent allowance of Mr. Abhijeet for the A.Y. 2023-24 :

| Particulars | Details | Amount | Amount |
|--|---------|--------|---------------|
| House Rent Allowance Received (from 1.4.2022 to 30.6.2022) | | 12,000 | |
| Less : Minimum of the following being exempted u/s 10(13A) | | | |
| a) Actual Amount Received | 12,000 | | |
| b) 40% of Salary [(Rs.5,000 + Rs.2,000) x 3] | 8,400 | | |
| c) Rent paid – 10% of salary (Rs.12,000 – Rs.2,100) | 9,900 | 8,400 | 3,600 |
| House Rent Allowance Received (from 1.7.2022 to 30.9.2022) | | 12,000 | |
| Less : Minimum of the following being exempted u/s 10(13A) | | | |
| a) Actual Amount Received | 12,000 | | |
| b) 40% of Salary [(Rs.6,000 + Rs.2,000) x 3] | 9,600 | | |
| c) Rent paid – 10% of salary (Rs.12,000 – Rs.2,400) | 9,600 | 9,600 | 2,400 |
| House Rent Allowance Received (from 1.10.2022 to 31.12.2022) | | 12,000 | |
| Less : Minimum of the following being exempted u/s 10(13A) | | | |
| a) Actual Amount Received | 12,000 | | |
| b) 50% of Salary [(Rs.6,000 + Rs.2,000) x 3] | 12,000 | | |
| c) Rent paid – 10% of salary (Rs.12,000 – Rs.2,400) | 9,600 | 9,600 | 2,400 |
| House Rent Allowance Received (from 1.1.2023 to 31.3.2023) | | | |
| (Fully taxable as assessee resides in his own house) | | | 12,000 |
| Taxable House Rent Allowance | | | 20,400 |

Question 4: Computation of taxable HRA and Gross Salary: Mr. Mohit is employed with XY Ltd. on a basic salary of Rs.10,000 p.m He is also entitled to Dearness allowance @100% of basic salary, 50% of which is included in salary as per terms of employment The company gives him house rent allowance of Rs.6,000 p.m, which was increased to Rs.7,000 pm with effect from 01-01-2023 He also got an increment of Rs1,000 p.m in his basic salary with effect from 01-02 2023 Rent paid by him during the previous' year 2022-23 is as under

April and May, 2022.

Nil, as he stayed with his parents

June to October, 2022

Rs.6,000 p m for an accommodation in Ghaziabad

November, 2022 to March, 2023

Rs 8,000 pm for an accommodation in Delhi

Compute his gross salary for assessment year 2023.24

(8 Marks, IPCC May 2012)

Solution: Computation of HRA exempt (amount in Rs):

| Period | 01.04.2022 To 31.05.2022 | 01.06.2022 to 31.10.2022 | 01.11.2022 to 31.12.2022 | 01.01.2023 to 31.01.2023 | 01.02.2023 to 31.03.2023 |
|---|--------------------------------|--------------------------------|--------------------------------|--------------------------------|--------------------------------|
| Number of months | 2 | 5 | 2 | 1 | 2 |
| Basic salary per month | 10,000 | 10,000 | 10,000 | 10,000 | 11,000 |
| Dearness allowance, to the extent it forms part of salary @ 100% of basic salary, 50% of which is included in salary as per terms of employment | 5,000 | 5,000 | 5,000 | 5,000 | 5,500 |
| Salary for the purpose of HRA exemption | 15,000 | 15,000 | 15,000 | 15,000 | 15,000 |
| Rent paid per month | - | 6,000 | 8,000 | 8,000 | 8,000 |
| HRA received | 6,000 | 6,000 | 6,000 | 7,000 | 7,000 |
| HRA is exempt per month upto least of following | | | | | |
| (a) HRA received | 6,000 | 6,000 | 6,000 | 7,000 | 7,000 |
| (b) Rent paid --10% of salary | - | 4,500 | 6,500 | 6,500 | 6,350 |
| (c) 40% of salary (50% of salary, for Delhi w.e.f. 1-1-2022) | 6,000 | 6,000 | 7,500 | 7,500 | 8,250 |
| HRA exempt p.m. = Least of the above three (a), (b) or (c) | - | 4,500 | 6,000 | 6,500 | 6,350 |
| Taxable HRA P.M | 6,000 | 1,500 | - | 500 | 650 |
| Total taxable HRA | 12,000 | 7,500 | - | 500 | 1300 |
| Total taxable HRA | 21,300 | | | | |

Computation of gross salary (Rs.)

| | |
|--|----------|
| Basic salary[Rs.10,000 + 10 + Rs.11.000x2] | 1,22,000 |
|--|----------|

| | |
|--|----------|
| Dearness allowance@100%of basic salary | 1,22,000 |
| House rent allowance | 21,300 |
| Gross salary | 2,65,300 |

Different allowances their taxability

There are many allowances some of which are **fully taxable**, some are **partially taxable** and some are **wholly exempt** from tax.

(1) Fully Taxable Allowances

- dearness allowance;
- City Compensatory allowance;
- Non-practicing Allowance
- Warden allowance;
- Project allowance;
- Family allowance;
- Medical allowance;
- Transport allowance to employee other than blind / deaf and dumb / orthopedically handicapped employee
- Any other cash allowance etc.

(2) Partly Taxable Allowances

(a) Allowances exempt from tax to the extent of amount expended for the purpose for which they are given Section 10(14)(i)] Allowances granted to meet expenses wholly, necessarily and exclusively incurred in the performance of the duties of an office or employment of profit, to the extent such expenses are actually incurred for that purpose:

- (i) Travelling Allowance** to meet cost of travel on tour or on transfer (including any sum paid in connection with transfer, packing and transportation of personal effects on such transfer).
- (ii) Daily Allowance** granted on tour or for the period of journey in connection with transfer, to meet ordinary daily charges incurred on account of absence from his normal place of duty.
- (iii) Conveyance Allowance** to meet expenditure incurred on conveyance in performance of official duties if free conveyance is not provided by the employer.
- (iv) Uniform Allowance** to meet expenditure incurred on purchase or maintenance of uniform or wears during the performance of the duties of an office or employment of profit.
- (v) Research Allowance** for encouraging the academic, research and training pursuits in educational and research institutions.
- (vi) Helper Allowance** to meet expenditure incurred on a helper where such helper is engaged for performance of official duties or employment of profit.

Note: An employee, being an assessee, who opts for the provisions of section 115BAC would be entitled for exemption only in respect of travelling allowance, daily allowance and conveyance allowance mentioned in (i) to (iii) above.

(b) Allowances exempt from tax to the extent of amount notified in the Rules [Section 10(14) (ii)]: Allowances granted to the assessee either to meet his personal expenses at the place where the duties of his office or employment of profit are ordinarily performed by him or at the place

where he ordinarily resides, or to compensate him for the increased cost of living, to the extent as may be prescribed -

| | Allowances | Amount exempt |
|------|---|---|
| (1) | Any Special Compensatory Allowance in the nature of Special Compensatory (Hilly Areas) Allowance or High Altitude Allowance or Uncongenial Climate Allowance or Snow Bound Area Allowance or Avalanche Allowance | Rs.800 or Rs. 7,000 or Rs.1300 per month depending upon the specified locations |
| (2) | Any Special Compensatory Allowance in the nature of border area allowance or remote locality allowance or difficult area allowance or disturbed area allowance | Rs.1,300 or Rs.1,100 or Rs. 1,050 or Rs.750 or Rs.300 or Rs.200 per month depending upon the specified locations. |
| (3) | Transport allowance to employees of Transport System: Allowance granted to an employee working in transport system to meet his personal expenditure incurred in course of his official duty of running the transport from one place to another, provided he is not in receipt of daily allowance. | (i) 70% of such allowance; or (ii) Rs.10,000 p.m Whichever is lower |
| (4) | Tribal Area Allowance: [in states of MP, Tamil Nadu, UP, Karnataka, Tripura, Assam, West Bengal, Bihar, Orissa] | Rs.200 P.M |
| (5) | Transport Allowance: Transport allowance granted to an employee, who is blind or deaf and dumb or orthopaedically handicapped for commuting between the place of residence and the place of duty | Rs.3,200 P.M |
| (6) | Underground Allowance: It is granted to the employees working in unnatural climate in underground mines | Rs.800 P.m |
| (7) | Children education allowance | Rs.100 P.m per child for maximum 2 children |
| (8) | Hostel expenditure allowance | Rs.300 p.m perchild for maximum 2 children |
| (9) | Compensatory field area allowance | Rs. 2600 per month in specified areas |
| (10) | Compensatory modified field area allowance | Rs.1000 per month in specified areas |
| (11) | Any special allowance in the nature of counter insurgency allowance granted to the members of the armed forces operating in areas away from their permanent locations, | Rs.3,900 per month |

| |
|---|
| Any assessee claiming exemption in respect of allowances mentioned at serial numbers 9, 10 and 11 shall not be entitled to exemption in respect of the allowance referred to at serial number 2 |
|---|

Note: An employee, being an assessee, who opts for the provisions of section 15BAC would be entitled for exemption only in respect of transport allowance granted to an employee who is blind or deaf and dumb or orthopedically handicapped with disability of the lower extremities of the body to the extent of Rs.3,200 p.m.

(3) Wholly Exempt Allowances:

- (a)** Allowances to Indian citizen who is a government employee and rendering services outside India [Sec. 10(7)].
- (b)** Allowances to High Court judges.
- (c)** Sumptuary Allowance to judges of High Court and Supreme Court,
- (d)** Allowances; to employees of UNO.

Question 5: Transport to employee of transport system: Examine with brief reasons whether the following is chargeable to income tax and the amount liable to tax with reference to the provisions of the Income-tax Act 1961: Allowance received by an employee Mr. Ram working in a transport system at Rs.12,000 p.m which has been granted to meet his personal expenditure while on duty. He is not in receipt of any daily allowance from his employer. **(2 Marks; Nov. 2018-NS)**

Solution: Under section 10(14), any allowance granted to an employee working in a transport system to meet his personal expenditure during his duty is exempt provided he is not in receipt of daily allowance. The exemption is 70% of such allowance (i.e., Rs.8,400 per month, being 70% of Rs.12,000) or Rs.10,000 per month, whichever is less. Hence Rs.8,400 p.m. is allowable as exemption u/s 10(14); and the balance Rs.3,600 p.m. shall be taxable. Hence taxable allowance will be Rs.3,600 x 12 Rs. 43,200.

2. TAXABILITY OF PERQUISITES

“Perquisites” as per Section 17(2).

The term **“perquisites”** means any extra benefit granted to the employee in addition to his salary. It may be given in cash or kind.

Perquisites [Section 17(2)]: It includes-

| | | |
|-----------|---|--|
| 1) | Rent free accommodation | the value of rent-free accommodation provided to the assessee by his employer. |
| 2) | Accommodation provided at concessional rate | the value of any concession in the matter of rent in respect of any accommodation provided to the assessee by his employer. |
| 3) | Perquisites taxable in case of specified employee | the value of any benefit or amenity granted or provided free of cost or at concessional rate to specified employees. |
| 4) | Employee’s obligation met by employer | Any sum paid by the employer in respect of any obligation, for which such payment would have been payable by the assessee [other than tax exempt under section 10(10CC). |

| | | |
|----|---|---|
| 5) | Life insurance/annuity contract payments | Any sum payable by the employer, whether directly or through a fund other than a RPF or an approved Superannuation fund (or a Deposit-linked Insurance Fund), to effect an assurance on the life of the assessee or to effect a contract for an annuity. |
| 6) | ESOP/ Sweat equity shares | The value of any specified security or sweat equity shares allotted or transferred, directly or indirectly, by the employer, or former employer, free of cost or at concessional rate to the assessee. |
| 7) | Contribution to RPP/ NPS/ Approved superannuation fund | the amount or the aggregate of amounts of any contribution made to the account of the assessee (a) in a recognised provident fund; (b) in the scheme referred to in Section 80CCD(1) and (c) in an approved superannuation fund, to the extent it exceeds Rs.7,50,000 in a previous year. |
| 8) | Interest /Dividend etc. on taxable contributions under RPF NPS/Approved Superannuation Fund | The annual accretion by way of interest, dividend or any other amount of similar nature during the previous year to the balance at the credit of the fund or scheme referred above to the extent it relates to the contribution which is included in total income in any previous year computed in such manner as may be prescribed. |
| 9) | Other fringe benefits | The value of any other fringe benefit or amenity as may be prescribed. The following perquisites have been specified — <ul style="list-style-type: none"> ➤ Interest-free or concessional loan; ➤ Travelling, touring for holiday; ➤ Food and beverage facility; ➤ Gifts; ➤ Credit card facility; ➤ Club facility; ➤ Use of movable asset; ➤ Sale of movable assets at concessional rates; and ➤ Other facilities |

Specified Employee and perquisites are taxable in case of specified employees.

(1) Specified Employee [Section 17(2)(iii)]:“Specified Employee” means —

- (a)** An employee who is a director of the company; or
- (b)** An employee being a person who has a substantial interest in the company i.e. who is the beneficial owner of equity shares carrying 20% or more of the voting rights in the company; or
- (c)** Any other employee whose income chargeable under the head “Salaries” (whether 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, exceeds Rs. 50,000.

In other words, while computing limit of Rs. 50,000, following shall be deducted/excluded

- (i) All non-monetary benefits;
- (ii) All monetary payments exempt under section 10
- (iii) Deductions under section 16[i.e. Standard deduction, Entertainment allowance and professional tax].

(2) Perquisites taxable in case of specified employees only: Car Facility, Provision for sweeper, domestic servant, Facility for gas, electricity, or water; Education facility; and 'transport facility are taxable only in the case of specified employees.

Question 6: Mr. M is an area manager of M/s. N. Steels Co. Ltd. During the previous year 2022-23 he gets following emoluments from his employer

| | |
|--|-----------------------------|
| Basic salary | Rs. 49,00,000 |
| Dearness Allowance [50% of basic salary forming part of retirement benefits] | Rs. 20,00,000 |
| Contribution to recognized-provident fund | 12% of basic salary and D.A |
| Contribution to superannuation fund | Rs. 2,00,000 |

Determine his gross salary for the Assessment Year 2023-24.

Solution: Computation of income from salary of Mr. M (amount in Rs.):

| | | |
|---|----------|-----------|
| Basic salary | | 40,00,000 |
| Dearness Allowance | | 20,00,000 |
| Employer's contribution to RPF [12% of salary (i.e., 12% of Rs. 50,00,000)] | 6,00,000 | |
| Contribution to approved superannuation fund | 2,00,000 | |
| Aggregate contribution to RPF and Approved superannuation fund | 8,00,000 | |
| Less: Exempt | 7,50,000 | 50,000 |
| Gross salary | | 60,50,000 |

Rent Free Accommodation (RFA)

Meaning of Accommodation [Explanations to Section 17(2) read with Rule 3] As per Rule 3, "accommodation" includes a house, flat, farmhouse or part thereof or accommodation in a hotel, motel, service apartment, guesthouse, caravan, mobile home, ship or other floating structure.

Valuation of Rent Free Accommodation: The value of residential accommodation provided by the employer directly or indirectly to the assessee or to any member of his household by reason of his employment, shall be determined in the following manner:

| | Circumstances | When accommodation is unfurnished | When accommodation is furnished |
|----|---|--|--|
| 1. | When accommodation is provided by the Government to its employees holding office/post in connection with Government affairs | License fee determined by the Government as reduced by the rent actually paid by the employee. | Value calculated under column 3) as increased by — 10% p.a. of the cost of furniture if owned by employer or actual hire charges payable in case the furniture is taken on hire. Any charges recovered from the employee shall be deducted. |

| | | | |
|----|--|---|---|
| 2. | (a) When the accommodation is provided by any employer and such accommodation is owned by the employer | <p>(i) in cities having population exceeding 25 lakhs as per 2001 census: 15% of salary</p> <p>(ii) In cities having population exceeding 10 lakhs but not exceeding 25 lakhs: 10% of salary</p> <p>(iii) In cities having population not exceeding 10 lakhs: 7.5% of salary</p> <p>Any amount recovered from the employee shall be reduce</p> | Value calculated under column (3) as increased by — 10% p.a. of the cost of furniture if owned by employer or actual hire charges payable in case the furniture is taken on hire. Any charges recovered from the employee shall be deducted, |
| | (b) Such accommodation is taken on lease or rent by the employer | <p>lower of</p> <p>(i) actual rent paid by the employer; or</p> <p>(ii) 15% of salary</p> <p>Any amount recovered from the employee shall be reduced</p> | Value calculated under column 3) as increased by — 10% p.a. of the cost of furniture if owned by employer or actual hire charges payable in case the furniture is taken on hire. Any charges recovered from the employee shall be deducted, |
| 3. | When the accommodation is provided by the above employers in a hotel | Not applicable | Lower of - <p>(i) the actual charges paid / payable to such hotel; or</p> <p>(ii) 24% of salary;</p> <p>Any amount recovered from employee shall be reduced.</p> |

Notes:

1) Salary= Basic pay + Dearness allowance/pay (if forms part of superannuation or retirement benefits) + Bonus + Commission + Fees + All taxable allowances + all monetary payments chargeable to tax; **from one or more employers.**

Salary does not include -

- (a) dearness allowance or dearness pay unless it enters into the computation of superannuation or retirement benefit of the employee concerned;
- (b) Employer's contribution to the provident fund account of the employee;
- (c) allowances which are exempted from payment of tax;
- (d) the value of perquisites specified under section 17(2);
- (e) any payment or expenditure specifically excluded under proviso to Section 17(2)(iii) or proviso to Sec. 17(2);
- (f) lump sum payments received at the time of termination of service or superannuation or voluntary retirement, like gratuity, severance pay, leave encashment, voluntary retrenchment benefits, commutation of pension and similar payments.

2) Exemption: The perquisite shall be exempt in the following cases—

(a) Hotel accommodation not exceeding 15 days: When the employee is provided accommodation in a hotel for a period not exceeding 15 days on account of his transfer from one place to another, then the value of such perquisite shall be Nil.

(b) Accommodation of temporary nature / remote area: Accommodation provided to employee working at mining site or an onshore oil exploration site, or a project execution site or a dam site or a power generation site or an offshore site —

(i) which, being of a temporary nature and having plinth area not exceeding 800 sq. feet is located not less than 8 kms. away from the local limits of any municipality or a cantonment board; or

(ii) which is located in a remote area. [‘Remote area’ means an area that is located at least 40 kilometres away from a town having a population not exceeding Rs.20,000 based on latest published all-India census.]

3) Double accommodation on account of transfer: Where on account of his transfer from one place to another, the employee is provided with accommodation at the new place of posting while retaining the accommodation at the other place, the value of perquisite shall be determined as follows -

| | | |
|-------------|--------------------------|--|
| (i) | For First 90 days | The value of perquisite shall be the value of such accommodation whose value is lower. When computed as per the above rules. |
| (ii) | After 90 days | The value of perquisite shall be aggregate of the value of both such accommodations as per the above rules.- |

4) Government Employees sent on deputation - Valuation: Where the accommodation is provided by the Central Government or any State Government to an employee who is serving on deputation with any body or undertaking under the control of such Government,

(a) the employer of such an employee shall be deemed to be that body or undertaking where the employee is serving on deputation; and

(b) the value of perquisite of such an accommodation shall be the amount calculated as if the accommodation is owned by the employer.

Question 7 :Mr. Chauhan has the following salary structure :

- Basic Salary Rs.5,000 p.m.
- Entertainment Allowance Rs.1,000 p.m.
- Education Allowance Rs.500 p.m. (he has 3 children)
- d) DA Rs.3,000 p.m.
- Fees Rs.5,000 p.a.
- Bonus Rs.10,000 p.a.
- Professional tax of employee paid by employer Rs.2,000 for the year
- He has been provided a rent-free accommodation in Mumbai.
- 60% of DA only forms part of retirement benefits

Compute taxable value of accommodation in the hands of Mr. Chauhan in the following cases :

I) The employer owns such accommodation.

II) The employer hires such accommodation at a monthly rent of Rs.900.

Solution:

Taxable value of rent-free accommodation for the A.Y. 2023-24 :

| Particulars | Basis of determination | Taxable Perquisite |
|-----------------------|---|--------------------|
| i) Owned by employer | 15% of Salary (Working) | Rs.16,830 |
| ii) Hired by employer | 15% of Salary or Actual rent paid by employer, whichever is lower | Rs.10,800 |

Working : Salary for the purpose of Rent-free accommodation :

| Particulars | Details | Amount | Amount |
|-----------------------------|---------------------|--------|-----------------|
| Basic Salary | | | 60,000 |
| Bonus | | | 10,000 |
| Fees | | | 5,000 |
| Allowances | | | |
| Dearness allowance | Rs.36,000 x 60% | 21,600 | |
| Entertainment Allowance | | 12,000 | |
| Education Allowance | Rs.6,000 – Rs.2,400 | 3,600 | 37,200 |
| Gross Taxable Salary | | | 1,12,200 |

Note : Professional tax paid on behalf of employee is a perquisite; hence the same shall not be included in salary for the aforesaid purpose.

Question 8:

Miss Stuti has the following salary structure :

| | Rs. |
|--------------------------------------|---|
| a) Basic salary | 15,000 p.m. |
| b) Dearness Allowance | 5,000 p.m. (not forming part of retirement benefit) |
| c) Hostel Allowance | 1,000 p.m. (does not have any child) |
| d) Tiffin Allowance | 500 p.m. |
| e) Transport Allowance | 200 p.m. |
| f) Bonus | 20,000 p.a. |
| g) Commission | 15,000 p.a. |
| h) Free refreshment in office worth | 5,000 p.a. |
| i) Mobile phone facility by employer | 900 p.m. |
| j) Computer facility worth | 10,000 p.a. |

She has been provided a Rent-free Accommodation (owned by employer) in Kolkata. The house was allotted to her with effect from 1/5/2022 but she could occupy the same only from 1/6/2022. Find her gross taxable salary.

Solution:

Computation of gross taxable salary of Miss Stuti for the A.Y. 2023-24 :

| Particulars | Details | Amount | Amount |
|--|---------|--------|-----------------|
| Basic Salary | | | 1,80,000 |
| Bonus | | | 20,000 |
| Commission | | | 15,000 |
| Allowances : | | | |
| Dearness Allowance | | 60,000 | |
| Hostel Allowance (Fully taxable as she has no child) | | 12,000 | |
| Tiffin Allowance | | 6,000 | |
| Transport Allowance | | 2,400 | 80,400 |
| Perquisite u/s 17(2) : | | | |
| Free Refreshment (not taxable) | | Nil | |
| Mobile or telephone facility | | Nil | |
| Computer facility | | Nil | |
| Rent Free Accommodation | Working | 29,425 | 29,425 |
| Gross Salary | | | 3,24,825 |

Working : Salary for the purpose of rent-free accommodation :

| | |
|--|----------|
| Basic Salary | 1,80,000 |
| Bonus | 20,000 |
| Commission | 15,000 |
| Allowances | |
| Dearness allowance | Nil |
| Hostel Allowance | 12,000 |
| Tiffin Allowance | 6,000 |
| Transport Allowance | 2,400 |
| Total | 2,35,400 |
| Value of Rent-Free Accommodation (being 15% x Rs.2,35,400 x 10/12) | 29,425 |

Question 9:

Sri Ashutosh has been provided with a furnished accommodation in a city having population of 14,00,000 as per 1,00,000. His salary details are as under :

| | |
|--|---|
| Basic | 25,000 p.m. |
| Allowance for increased cost of living | 5,000 p.m. |
| Children Education allowance | 3,000 p.m. [He has one son and two married daughters] |

Furniture details as under :

| Particulars | Hired by the employer (Hire charge) | Owned by the employer (Original Cost) |
|-----------------|--|--|
| T.V. | 2,000 p.a. | - |
| Refrigerator | - | 10,000 |
| Washing Machine | - | 5,000 |
| Other furniture | 1,000 p.m. | 20,000 |

Calculate gross taxable salary of Sri Ashutosh for the A.Y. 2023-24.

Solution:

Computation of gross taxable salary of Sri Ashutosh for the A.Y. 2023-24:

| Particulars | Amount | Amount |
|---|--------|-----------------|
| Basic Salary | | 3,00,000 |
| Dearness allowance (Allowance for increased cost of living) | | 60,000 |
| Children Education Allowance | 36,000 | |
| Less : Exemption (Rs.100 x 2 x 12) | 2,400 | 33,600 |
| Rent Free Furnished Accommodation | | |
| Value of Accommodation (10% of Salary ¹) | 39,360 | |
| Value of furniture ² | 17,500 | 56,860 |
| Gross Taxable Salary | | 4,50,460 |

1. Salary for valuation of rent- free accommodation:

| | |
|---------------------|-----------------|
| Basic Salary | 3,00,000 |
| Dearness allowance | 60,000 |
| Education Allowance | 33,600 |
| Total | 3,93,600 |

2

| Furniture | Perquisite for hired furniture | Perquisite for owned furniture | Total Taxable value of furniture |
|-----------------|--------------------------------|--------------------------------|----------------------------------|
| T.V. | 2,000 | - | 2,000 |
| Refrigerator | - | 10% of 10,000 | 1,000 |
| Washing Machine | - | 10% of 5,000 | 500 |
| Other furniture | 12,000 | 10% of 20,000 | 14,000 |
| Total | | | 17,500 |

Municipal value and Fair rent are irrelevant

Perquisites taxable in the hands of specified employees:

The following perquisites shall be taxable in the hands of specified employees only. However, if bills are in the name of employee or obligation to make payment is on the employee, then the reimbursement of expenses shall be taxable in case of all employees under section 172)(iv).

(1) Motor car or other conveyance facility: The rules for valuation of perquisite in respect of use of conveyance provided to an employee or any member of his household are as follows -

| Circumstances (Col.1) | Used wholly for private purposes (Col.2) | Partly for official and partly for private purposes(Col.3) | |
|--|--|--|--|
| I. When motor car is owned or hired by the employer — | | | |
| (a) When maintenance and running expenses are met or reimbursed by employer | Amount incurred or re-imbursed by employer + Chauffeur's salary + Normal wear & tear @ 10% p.a. of | If cubic capacity does not exceed 1.6 litres: Rs.1,800 p.m. (plus Rs.900 p.m. if chauffeur | If cubic capacity exceeds 1.6 litres Rs.2,400 p.m. (plus Rs.900 p.m. if |

| | | | |
|--|---|---|---|
| | actual cost of car or hire charges - Amount recovered from employee | is provided) [Note 4] | chauffeur is provided) [Note 4] |
| (b) When maintenance and running expenses are met by employee. [See note1] | Normal wear and tear @ 10% p.a. of the actual cost of the car or hire charges. | If cubic capacity does not exceed 1.6 litres: Rs.600 p.m. (plus Rs.900 p.m. if chauffeur is provided) (Note 41) | If cubic capacity exceeds 1.6 litres: Rs.900 p.m. (plus Rs.900 p.m. if chauffeur is provided) [Note 4] |
| II. Where motor car is owned by employee and, maintenance and running expenses including remuneration of the chauffeur are met or reimbursed by the employer. | Actual expenditure incurred by employer Less: Amount, if any, paid or recovered from the employee, | Actual expenses incurred by employer Less: if cubic capacity of engine does not exceed 1.6 litres: Rs.1,800 p.m. (plus Rs. 900 if chauffeur is also provided) [Note 3] | Actual expenses incurred by employer Less: If cubic capacity of engine exceeds 1.6 litres: Rs.2,400 p.m. (plus Rs.900 if chauffeur is also provided). [Note 3] |
| III. Conveyance other than motorcar (Scooter, motorcycle etc.), is owned by the employee and the employer meets its running expenses | Amount actually incurred by employer for maintenance and running less Amount recovered from employee | Actual expenditure incurred by the employer less Rs.900 p.m. [Note 3] | |

Notes —

- (1)** If conveyance is used wholly and exclusively for the purpose of business, then it will be fully exempt as the same is not a prerequisite.
- (2)** In case more than one car is provided to the employee (not wholly for official purpose), then one car is to be considered as partly official and partly for personal purpose; and the other to be considered as wholly for private purposes.
- (3)** Where the assessee claims that —
 - (a)** the conveyance is used wholly and exclusively for official purposes; or
 - (b)** expenses incurred on running and maintenance of the conveyance owned by him is higher than the amounts deducted in items (II) and (III), then—
 - he may claim for such higher amount provided—
 - (i)** the employer has maintained full details of journey undertaken for official purpose including date of journey, destination, mileage, and expenditure incurred thereon; and

(ii) the employer gives a certificate to the effect that the claimed expenditure was spent wholly and exclusively for official purposes.

(4) In these cases, no deduction shall be allowed to the employee for the amount recovered from him.

(5) **Month:** The perquisite is valued for each calendar month. Calendar month is the month starting from any particular date of a month but ending on a date immediately preceding the corresponding date of next month. Eg: 15th July to 14th August constitute a calendar month.

(6) in case if car is used for commuting between office and residence, then it shall be considered as official use.

(2) **Sweeper, gardener, watchman or personal attendant:** If any sweeper, gardener, watchman or personal attendant is provided to an employee or any of his household member, then the value shall be Salary paid or payable to such person less amount recovered from the employee, if any.

(3) **Gas, electricity or water facility:** The value of perquisites shall be -

(i) **if supplied by employer from his own sources:** Manufacturing cost per unit x Number of units consumed by employee

(ii) **if taken by employer from outside agencies:** hire charges paid to such agencies.

Note: If any amount is recovered from the employee the same shall be reduced to arrive at taxable value, if any

(4) **Free or Concessional educational facility:**

| Circumstance | Valuation of perquisite |
|--|--|
| (a) Employer incurs cost of education. | Actual expenditure incurred by the employer. |
| (b) | Cost of such education in a similar institution in or near the locality. |
| (i) Educational institution is owned and maintained by the employer; or | The perquisite is exempt if |
| (ii) Free educational facility is provided in any other institution by reason of his employment with that employer | (a) free education facility is provided to children of the employee and (b) cost of education is upto Rs.1,000 p.m. per child, otherwise it is fully taxable. |
| Note: Any amount paid or recovered from the employee shall be reduced from value of perquisite. | |

Transport facility to the employees of transport undertaking: If any transport facility is provided by an employer carrying transport business (of carrying passengers / goods) to his employee in a conveyance owned, leased or made available by some arrangement, then-

Taxable Value = Amount charged from general public for such facility less amount recovered from the employee, if any.

Exemption: This rule shall not apply to employees of an airline or the railways.

Question 10

Mr. Piyush has been provided a car (1.5 ltr.) on 15/7/2022. The cost of car to the employer was Rs.6,00,000 and maintenance cost incurred by employer Rs.20,000 p.a. Chauffeur salary paid by employer (Mr. Ratan) Rs.4,000 p.m. The car is 40% used for office and 60% for personal purpose. Charges paid by employee for such facility Rs.5,000 p.a. Find taxable value of perquisite.

Solution:

Taxable value of perquisite :

| Particulars | Details | Amount |
|---------------------------|--------------|---------------|
| Car | Rs.1,800 × 8 | 4,400 |
| Driver | Rs.900 × 8 | 7,200 |
| Taxable Perquisite | | 21,600 |

1. A part of month shall not be considered for this purpose.
2. Whenever statutory value is taken as taxable value of perquisite then amount charged from employee shall not be subtracted.

Question 11:

Wasim has a car (1.5 ltr.) used for office as well as for personal purpose. During the year car is used 80% for business purpose being certified by the employer. During the year, he incurred Rs.50,000 on maintenance and running of such car. The entire cost is reimbursed by the employer. Find taxable perquisite if assessee wish to claim higher deduction, when – (a) A proper log book is maintained; (b) A proper log book is not maintained

Solution :**a. When log book is maintained**

Taxable perquisite in the hands of Wasim

Actual expenditure incurred by the employer is reduced to the extent it is used for office purpose, as a proper record is kept and duly certified by employer.

Amount reimbursed by the employer Rs.50,000

Less : Deduction (80% of Rs.50,000) Rs.40,000

Taxable amount Rs.10,000**b. When log book is not maintained**

Taxable perquisite in the hands of Wasim

Actual expenditure incurred by the employer is reduced to the extent of Rs.1,800 p.m. even though it is used for office purpose but a proper record is not kept.

Amount reimbursed by the employer Rs.50,000

Less : Deduction (Rs.1,800 x 12) Rs. 21,600

Taxable amount Rs.28,400**Question 12:**

Mr. Vijay, manager, has been provided the following car facilities by Kishan Ltd. (his employer) :

| Particulars | Car A | Car B | Car C |
|--|------------------------------------|----------|------------------|
| Owned by | Employer | Employer | Employer |
| Used for | Office as well as personal purpose | | Personal purpose |
| Cost of car | 3,00,000 | 5,00,000 | 2,00,000 |
| Maintenance expenditure incurred by employer | 50,000 | 60,000 | - |
| Maintenance expenditure incurred by employee | - | - | 40,000 |

| | | | |
|-----------------|----------|----------|----------|
| Capacity of car | 1.8 ltr. | 1.4 ltr. | 1.6 ltr. |
|-----------------|----------|----------|----------|

Find taxable value of car facility.

Case a) Mr. Vijay holds 17% of equity share capital and 30% of preference share capital of Kishan Ltd. and his wife holds 13% equity share capital of the same company. Assume his total salary during the year other than perquisite is Rs.40,000;

Case b) Mr. Vijay holds 25% equity share capital of the employer company.

Solution :

Case a) Since Mr. Vijay is not a specified employee & employer owns all cars therefore car facility shall not be taxable.

Case b) Since Mr. Vijay holds substantial interest in employer-company hence he is a specified employee.

As employee has been provided 2 cars, used for office as well as for personal purpose, therefore he will have to opt one car as for 'office as well as personal purpose' & the other car for personal purpose. In the given case, assessee has two options -

Option 1) Car A is used for office as well as personal purpose and car B is used for personal purpose.

Option 2) Car A is used for personal purpose and car B is used for office as well as personal purpose.

In any case, Car C is used for Personal purpose.

| Particulars | Workings | Option 1 | | | Option 2 | | |
|--------------|-----------------------------------|----------|----------|-----------------|----------|--------|-----------------|
| | | Car A | Car B | Car C | Car A | Car B | Car C |
| Car used for | | Both | Personal | Personal | Personal | Both | Personal |
| | Rs.2,400 x 12 | 28,800 | | | | | |
| | 10% of Rs.5,00,000 + Rs.60,000 | | 1,10,000 | | | | |
| | 10% of Rs.2,00,000 | | | 20,000 | | | 20,000 |
| | 10% of Rs.3,00,000 + Rs.50,000 | | | | 80,000 | | |
| | Rs.1,800 x 12 | | | | | 21,600 | |
| Total | | | | 1,58,800 | | | 1,21,600 |

As option 2 has lesser taxable value, hence assessee will opt for option 2 & taxable value shall be Rs.1,21,600.

Employee Stock Option Plan/ Scheme (ESOP) or Sweat Equity granted by an employer to his employee?

The taxable value of ESOP or any Specified Security granted by an employer to his employee shall be determined as under —

| | |
|--|-----|
| Fair market value (determined as per prescribed method) of the security or sweat equity shares - on the date on which the option is exercised by the assessee/employee | xxx |
| Less: Amount actually paid by, or recovered from, assessee in respect of such security or shares | xxx |
| Value of such security or sweat equity shares | xxx |

Notes:

- (1) "Sweat Equity Shares"** means equity shares issued by a company to its employees or directors at a discount or for consideration other than cash for providing know-how or making available rights in the nature of intellectual property rights or value additions, by whatever name called.
- (2) "Option"** means a right but not an obligation granted to an employee to apply for the specified security or sweat equity shares at a predetermined price.
- (3)** The taxability of Employee Stock Option Plan/ Scheme (ESOP) or Sweat Equity shall arise when the same is allotted or transferred, directly or indirectly, by the employer, or former employer.
- (4) Deferment of Taxability in case of ESOP allotted to employee of eligible start-up** Where the income of the assessee of any assessment year includes perquisite income of specified security or sweat equity shares and such specified security or sweat equity shares are allotted or transferred directly or indirectly by the current employer, being an eligible start-up referred to in section 80-IAC, the tax or interest on such income included in the notice of demand u/s 156(1) shall be payable by the assessee within 14 days —
 - (i)** after the expiry of 48 months from the end of the relevant assessment year; or
 - (ii)** from the date of the sale of such specified security or sweat equity share by the assessee; or
 - (iii)** from the date of the assessee ceasing to be the employee of the employer who allotted or transferred him such specified security or sweat equity share,

Whichever is the earliest.

Thus, the tax burden on such employees getting ESOP has been reduced by deferring the payment of tax by 5 years or till they leave the company or when they sell their shares, whichever is earliest.

FMV of the Employee Stock Option Plan/Scheme (ESOP) or Sweat Equity shares allotted or transferred shall be determined on the date of exercising the option as under

| | Case | Fair market value shall be |
|-----------|--|--|
| 1. | Listed equity shares: If, on the date of exercising of the option, the shares of the company are listed— <ul style="list-style-type: none">(a) on only one recognised stock exchange and shares are traded on that date on that exchange(b) on only one recognised stock exchange but shares are not traded on that date on that exchange . | (Opening price on that date on that stock exchange + Corresponding Closing Price)+ 2 Closing price of the share on that recognised stock exchange. on a immediately .preceding date closest to the date of exercising of the option. |
| | (a) on more than one recognised ,stock exchanges but shares are traded on that date on any of the exchanges | (Opening price on that date on stock exchange, which records the highest volume of trading in the in the share + corresponding Closing Price) +2. |
| | (b) on more than one recognized stock exchanges but shares are not traded on | Closing price of the share on any recognised stock exchange, which records the highest |

| | | |
|----|--|--|
| | that date on any, of the exchanges . | volume of trading in such. share as on immediately preceding date closest to the date of' exercising of the option. |
| 2. | Unlisted equity shares: If, on the date of exercising of option, shares of the company are not listed on any recognised exchange. | Such value of the share in company as determined by a Category I Merchant Banker registered with the SEBI on the specified date. |
| 3. | Specified security not being an equity share. | Such value as determined by a merchant banker on the specified date. |

Notes:

- (i) **Closing price** of a share on a recognised. stock exchange on a date means the price of the last settlement on such date on such stock exchange however where the stock exchange quotes both buy and sell prices, the 'sell price' shall be the closing price
- (ii) **Opening price** of a share on a recognised stock exchange on-a date means- the price of the first settlement on such stock exchange however, Where the stock exchange quotes both buy and sell prices, the sell price shall be the opening price.
- (iii) "Specified date" means —
- (a) date on which the option is exercised, or
- (b) any date earlier than the date of exercising the option provided such date is not more than 180 days earlier than ESOP the date of exercising the option.

Question 13:

A company 'X' grants option to its employee 'R' on 1st April, 2017 to apply for 100 shares of the company for making available right in the intellectual property to the employer-company at a pre-determined price of Rs.50 per share with date of vesting of the option being 1st April, 2018 and exercise period being 1st April, 2018 to 31st March, 2023. Employee 'R' exercises his option on 31st March, 2022 and shares are allotted/transferred to him on 3rd April, 2022.

Fair market value of such share on different dates are as under :

| | | | |
|-------------------|-------------------|-------------------|-------------------|
| 01-04-2017 | 01-04-2018 | 31-03-2022 | 03-04-2022 |
| Rs.100 | Rs.180 | Rs.440 | Rs.470 |

Compute taxable perquisite, if any, in hands of Mr. R for A.Y. 2023-24.

Solution :

Since shares are allotted by the company after 31-03-2022 (even though it is exercised by the employee on 31-03- 2022), hence, it is taxable in A.Y. 2023-24. Value of the perquisite is as under :

| Particulars | Amount |
|--|---------------|
| The FMV of shares on the date on which the option is exercised [Rs.440 x 100 shares] | 44,000 |
| Less : The amount actually paid by assessee in respect of such shares [Rs.50 x 100 shares] | 5,000 |
| Value of perquisite | 39,000 |

Note : For the purpose of computing capital gain on transfer of these shares by Mr. R, Rs.44,000 (i.e. Rs.440 per shares) shall be considered as cost of acquisition of such shares

Valuation of medical facilities provided by employer.

The medical facilities provided by an employer to his employee shall be valued as under[Proviso to Section 17(2)]

- (1) Treatment in hospital maintained by employer: Exempt:** The medical treatment of an employee or any of his family member in a hospital maintained by the employer is exempt from tax.
- (2) Treatment in government hospital — Exempt:** Any sum paid by an employer in respect of an expenditure incurred by the employee on his medical treatment or treatment of any of his family member, in a hospital maintained by the Government/local authority or any other hospital approved by Government, is exempt from tax.
- (3) Treatment Of prescribed disease in a hospital approved by the Principal Chief Commissioner or Chief Commissioner Exempt:** Any sum paid by an employer in respect of expenditure incurred on medical treatment of employee or any of his family member in respect of diseases or ailments prescribed in Rule 3A in. an approved hospital is exempt from tax.
- (4) Health insurance premium paid by the employer - Exempt:** Any premium paid by an employer in order to effect an insurance on the health of his employee, under any scheme approved by the Central Government or Insurance Regulatory and Development Authority (IRDA) for the purposes of Section 36(1)(ib), is exempt from tax.
- (5) Health insurance premium reimbursed by the employer - Exempt:** Any sum paid by the employer in order to reimburse the health insurance premium paid by employee on his health or on health of any of his family member, under a scheme approved by Central Government or IRDA under section 80D, is exempt from tax.
- (6) Medical treatment abroad:** Expenditure incurred or reimbursed by the employer for
 - (a)** Medical treatment of employee or his family member outside India and stay abroad of such employee or his family member for medical treatment and one attendant shall be exempt to the extent permitted by RBI; and
 - (b)** Cost of travel of employee or his family member and one attendant who accompanies the patient in connection with such treatment is exempt only if gross total income of such employee, as computed before including this expenditure, does not exceed Rs.2 lakh.

Hospital: Hospital includes a dispensary or a clinic or a nursing home;

Meaning of family: "Family" means - (i) spouse and children of that individual; and (ii) the parents, brothers and sisters of the individual or any of them wholly or mainly dependent on the individual.

Question 14: Medical Facility: Ms. Rakhi is an employee in a private company. She receives the following medical benefits from the company during the previous year 2022-23:

| | |
|--|-------|
| (1) Reimbursement of following Medical Expenses incurred by Ms. Rakhi — | |
| (a) On treatment of her self employed daughter in a private clinic | 4,000 |
| (b) On treatment of herself by Family doctor | 8,000 |
| (c) On treatment of her Mother-in-law dependent on her, in a Nursing Home | 5,000 |
| (2) Payment of premium on Mediclaim Policy taken on her health. | 7,500 |

| | |
|--|----------|
| (3) Medical Allowance. | 2000 P.M |
| (4) Medical Expenses Reimbursed on her Son's treatment in a Government Hospital. | 5,000 |
| (5) Expenses incurred by company on the treatment of her minor son abroad. | 1,05,000 |
| (6) Expenses in relation to Foreign Travel and stay of Rakhi and her son abroad for Medical Treatment. (Limit prescribed by RBI for this is Rs.2,00,000) | 1,20,000 |

Discuss about the taxability of above benefits and allowances in the hands of Rakhi.

(8 Marks, May 2014)

Solution: Computation of taxable value of perquisite in the hands of Ms. Rakhi (amount in Rs.)

| | | |
|---|--------------|---------------|
| Reimbursement of following Medical Expenses incurred by Ms. Rakhi. | | |
| (a) On treatment of her self employed daughter in a private clinic (The same shall be taxable,) | 4,000 | |
| (b) On treatment of herself by Family doctor (The same shall be taxable) Rs.8,000 | <u>8,000</u> | |
| Total expenditure | 12,000 | 12,000 |
| Less: Exempt | Nil | 5,000 |
| (c) On treatment of her Mother-in-law dependent on her, in a Nursing Home (Since mother in Rs.5,000 law is not his family member hence the same shall be taxable) | | Exempt |
| Payment of premium on Medclaim Policy taken on her health. (The same shall be exempt from tax) | | 24,000 |
| Medical Allowance (Fully taxable) | | Exempt |
| Medical Expenses Reimbursed on her Son's treatment in a Government Hospital | | Exempt |
| Expenses incurred by company on the treatment of her minor son abroad. [WN] | | Exempt |
| Expenses in relation to Foreign Travel and stay of Rakhi and her son abroad for Medical Exempt Treatment. [WN] | | |
| Taxable value of perquisite | | 41,000 |

Working Note: As per clause (vi) of the first proviso to section 17(2), the following expenditure incurred by the employer would be excluded from perquisite subject to certain conditions -

- (i) The expenditure on medical treatment and stay abroad would be excluded from perquisite to the extent permitted by Reserve Bank of India;
- (ii) The expenditure on travel would be excluded from perquisite only in the case of an employee whose gross total income, as computed before including the said expenditure, does not exceed Rs.2 lakh.

Assuming that the limit of Rs.2 lakh prescribed by RBI pertains to both expenditure on medical treatment of minor son as well as expenditure on stay abroad of Ms. Rakhi and her minor son, such expenditure would be excluded from perquisite subject to a maximum of Rs.2 lakh. If such expenditure is less than Rs.2 lakh, it would be fully excluded. The foreign travel expenditure of Ms. Rakhi and her minor son borne by the employer would be excluded from perquisite only if the gross total income of Ms. Rakhi, as computed before including the said expenditure, does not exceed Rs.2 lakh.

Question 15: Medical facility: Himalaya Ltd. reimburses the following expenditure on medical treatment of the son of an employee Karan. The treatment was done at UK:

- (i) Travelling expenses Rs 1,15,000.
- (ii) Stay expenses at UK permitted by RBI Rs.45,000 (Actual expenses Rs.70,000).
- (iii) Medical expenses permitted by RBI Rs50,000 (Actual expenses Rs.70,000).

Compute the taxable perquisites in the hands of Karan, if his annual income from salary after standard deduction was (i) Rs 1,55,000; (ii) Rs 1,56,000.

Solution: Computation of taxable value of medical perquisite (amount in Rs.)-

| | |
|---|---------------|
| In case salary is Rs1,55,000, taxable value of medical perquisite will be | |
| Stay expenses [Rs70,000 -Rs 45,000 (exempt)] | 25,000 |
| Medical expenses [Rs70,000 - Rs50,000 (exempt)] | 20,000 |
| Travelling expenses (See note) | nil |
| Taxable value of medical perquisite | 45,000 |

Note: The gross total income before including travel expenses = Rs.1,55,000 + Rs.25,000 + Rs.20,000 = Rs.2,00,000, i.e. does not exceed Rs. 2,00,000. Hence, the travel expenses will be taxable in this case.

| | |
|---|-----------------|
| In case 1,56,000, taxable value of medical perquisite will be | |
| Stay expenses [Rs.70,000 - Rs.45,000] | 25,000 |
| Medical expenses [Rs.70,000 - Rs.50,000] | 20,000 |
| Travelling expenses(see note) | 1,15,000 |
| Taxable value of medical perquisite | 1,60,000 |

Note: The gross total income before including travel expenses = Rs. 1,56,000 + Rs.25,000 + Rs. 20,000 = Rs.2,01,000, i.e. greater than 2 lakh. Hence, the travel expenses will be taxable in this case.

Valuation of prescribed Fringe Benefits:

Section 17(2)(vii) specifies that any fringe benefit or amenity provided to an employee shall be considered as 'perquisite'. The following benefits provided by the employer or by any other person on his behalf to the employee or any member of his household shall be valued as follows -

(1) Interest free or concessional loans: The value of benefit resulting from the loans made available to the employee or any member of their household shall be — (amount in Rs.)

| | |
|---|-----|
| Maximum outstanding monthly balance x Rate charged p.a. by SBI for similar purpose, as on 1 st day of relevant previous year (i.e. as on 1-4-2022 for assessment year 2023-24) | xxx |
| Less: Interest, if any, actually paid by or any such member of his household. | xxx |
| Maximum outstanding monthly balance means the aggregate outstanding balance for each loan as on the last day of each month. | |

- **Exemption:** The perquisite in respect of interest is exempt -
Where the amount of loans are petty not exceeding in the aggregate RS.20,000; or if such loans are made available for medical treatment in respect of diseases specified in Rule 3A.
- **No exemption:** In case of loan provided for medical treatment in respect of diseases specified in Rule 3A the exemption shall not apply to so much of the loan as has been reimbursed to the employee under any medical insurance scheme.

(2) Travelling, touring, accommodation and any other expenses paid for or borne or reimbursed by the employer for any holiday, other than leave travel concession, assistance, availed of by an employee or any member of his household: The perquisite shall be valued as the sum equal to the amount of the expenditure incurred by the employer in that behalf.

Notes:

(i) Valuation when facility is maintained by employer and is not available uniformly to all employees: Value of benefit = Value at which such facilities are offered by other agencies to the public.

(ii) If employee is on official tour and expenses are incurred for any member of his household accompanying him, the amount of expenditure so incurred shall also be a fringe benefit or amenity.

(iii) Where any official tour is extended as a vacation, the value of such fringe benefit will be limited to the expenses incurred in relation to such extended period of stay or vacation.

The amount so determined shall be reduced by the amount, if any paid or recovered from the employee for such benefit or amenity.

(3) Free food & non-alcoholic beverages provided by employer: Value of benefit = Amount of expenditure incurred by employer - Amount paid or recovered from the employee for such benefit or amenity.

Exemption The following will not be treated as perquisites -

(i) Free food and non-alcoholic beverages provided by employer during working hours at office or business premises or through paid vouchers which are not transferable and usable only at eating joints, to the extent the value thereof either case does not exceed Rs.50 per meal, the value exceeds Rs.50 per meal, the excess amount shall be taxable

(ii) Tea or snacks provided during working hours.

(iii) Free food and non-alcoholic beverages provided dining working hours in a remote area or an off-shore installation.

However, the exemption provided in respect of free food and non-alcoholic beverage provided by such employer through paid voucher shall not apply to an employee, being an assessee, who has exercised option under Section 115BAC.

(4) Gift including gift vouchers and tokens received by the employee or any member of his household on ceremonial occasions or otherwise: Value of benefit = Sum equal to amount of such gift.

Exemption: If the value of such gift or voucher or token less than Rs. 5,000 in aggregate during the previous year, the value of perquisite shall be taken as nil'; otherwise it is fully taxable.

(5) Credit card or Add on card provided to employee or any member of his household: Value of perquisite = Amount of such expenses (including the membership fees and annual fees) charged to such credit card or reimbursed by the employer - Amount paid or recovered from the employee.

Exemption: Perquisite is exempt if expenses are incurred wholly & exclusively for official purposes.*

(6) Club facility provided to employee or any member of his household: Value of benefit Actual expenditure (including the amount of annual or periodical fee)paid or reimbursed by the employer — Amount paid or recovered from the employee.

Exemption the perquisite shall be exempt in the following cases —

(i) Where the employer has obtained corporate membership of the club and the facility is enjoyed by the employee or any member of his household the initial fee paid for membership shall be exempt. -

(ii) If expenditure is incurred wholly & exclusively for business purposes it shall not be a perquisite.*

(iii) Use of health club, sports and similar facilities provided uniformly to all employees by the employer shall not be taxable as perquisites.

***Note for (5) and (6):** Where the expenses are claimed to be incurred wholly and exclusively for official purposes, the perquisite in (5) & (6) above shall be exempt only if the following conditions are fulfilled

- complete details in respect of such expenditure is maintained by the employer which may include the date of expenditure, the nature of expenditure and its business expediency; and
- the employer gives a certificate for such expenditure to the effect that the same was incurred wholly and exclusively for the performance of official duties.

(7) Use, by the employee or any member of his household, of movable assets (other than assets elsewhere specified in Rule 3) belonging to the employer or hired by him: The value of perquisite shall be 10% p.a. of the actual cost of such asset, or, amount of rent or hire charges paid or payable by the employer less amount paid or recovered from the employee.

Exemption Use of Laptops and computers belonging to or hired by the employer is exempt.

(8) Transfer of any movable asset which was belonging to the employer, directly or indirectly to employee or any member of his household: The value of benefit shall be calculated as follows:—

| Computers & electronic gadgets* | Motor cars | others |
|--|--|---|
| Actual cost Less: Depreciation @ 50% under Reducing Balance Method Less: Amount, if any, paid or recovered from the employee | Actual cost Less: Depreciation @ 20% under Reducing Balance Method Less: Amount, if any, paid or recovered from the employee | Actual cost Less: Depreciation @ 10% under Straight line Method Less: Amount, if any, paid or recovered from the employee |

Note:

(1) The deduction on account of depreciation (normal wear and tear) is allowed for each completed year during which such asset was put to use by the employer.

(2) *electronic gadgets in this case means data storage and handling devices like computer, digital diaries and printers. They do not include household appliance (i.e. white goods) like washing machines, microwave ovens, mixers, hot plates, ovens etc.

(9) Any other benefit or amenity: Value of any other benefit or amenity, service, right or privilege provided by the employer= Cost of the same to the employer under an arm's length transaction- Employee's contribution.

Exemption: if an employer pays/reimburses the telephone bills or mobile phone charges, then there will be no tax liability.

Note: Member of household shall include –

- (i) Spouse(s);
- (ii) Children and their spouses;
- (iii) Parents; and
- (iv) Servants and dependents.

Question 16: Transfer of movable assets: Find out the taxable value of perquisites from the following particulars in case of an employee to whom the following assets held by the company were sold on 13th September, 2022 **(amt in Rs.):**

| | Car | Laptop | Furniture |
|--------------------------------|----------|----------|-----------|
| cost of purchase (in May 2019) | 8,72,000 | 1,22,500 | 35,000 |
| Sale price | 5,15,000 | 25,000 | 10,000 |

The assets were put to use by the company from the day these were purchased.

Solution: Computation of taxable value of perquisite **(amounts in Rs.)**

| | Car (20%WDV) | Laptop (50%wdv) | furniture (10%slm) |
|--|-----------------|--------------------|-----------------------|
| Cost of the asset | 8,72,000 | 1,22,500 | 35,000 |
| Less: Depreciation for each completed year of use- | | | |
| 1 st year ending May 2021 | 1,74,400 | 61,250 | 3,500 |
| Balance as on 1 st June 2021 | 6,97,600 | 61,250 | 31,500 |
| 2 nd year ending May 2022 | 1,39,520 | 30,625 | 3,500 |
| Balance as on 1 st June 2022 | 5,58,080 | 30,625 | 28,000 |
| Less: sale price | 5,15,000 | 25,000 | 10,000 |
| Taxable value of perquisite | 43,080 | 5,625 | 18,000 |

Perquisites which are exempt from tax.

Ans: The following perquisites are exempt from tax in the hands of all employees.

| | Particulars | Explanation |
|----|---|---|
| 1. | Telephone | Telephone provided by an employer to an employee at his residence. |
| 2. | Transport Facility | Transport facility provided by an employer engaged in the business of carrying of passengers or goods to his employees either free of charge or at concessional rate. |
| 3. | Privilege passes and privilege ticket | Privilege passes and privilege ticket orders granted by Indian Railways to its employees. |
| 4. | Perquisites allowed outside India by the Government | Perquisites allowed outside India by the Government to a citizen of India for rendering services outside India. |
| 5. | Employer's contribution to staff group insurance scheme | Employer's contribution to staff group insurance scheme |
| 6. | Annual premium by employer on personal accident policy | Payment of annual premium by employer on personal accident policy effected by him on the life of the employee. |

| | | |
|-----|---------------------------------------|---|
| 7. | Refreshment | Refreshment- provided to all employees during working hours in office premises. |
| 8. | Subsidized lunch | Subsidized lunch or dinner provided to an employee. |
| 9. | Recreational facilities | Recreational facilities, including club facilities, extended to employees in general i.e., not restricted to a few select employees |
| 10. | Amount spent on training of employees | Amount spent by the employer on training of employees or amount paid for refresher management course including expenses on boarding and lodging. |
| 11. | Sum payable by employer to a RPF | Sum payable by an employer to a RPF or deposit-linked insurance fund established under the Coal Mines Provident Fund or the Employees Provident Fund Act. |
| 12. | Leave travel concession | Leave travel concession, subject to the conditions specified under section 10. |
| 13. | Medical facilities | Medical facilities subject to certain prescribed limits. |
| 14. | Rent –free official residence | Rent-free official residence provided to a Judge of a High Court or the supreme Court. |
| 15. | Rent-free furnished residence | Rent-free furnished residence Rent-free furnished residence including maintenance provided to an Officer of Parliament, Union Minister and a leader of Opposition in Parliament. |
| 16. | Conveyance facility | Conveyance facility Conveyance facility provided to High Court Judges under section 228 of the High Court Judges (Conditions of Service) Act 1954 and Supreme Court Judges under section 23A of the Supreme Court Judges (Conditions of Service) Act, 1958. |

Question 17:

Determine taxable perquisite in the following cases :

1. Miss Shradha received a wrist-watch of Rs.3,000 on 17/7/2022 and a golden chain worth Rs.12,000 on 18/8/2022 from her employer, Mr. Raju.
2. Miss Rakhi received Rs.11,000 cash–gift from her employer, Dipu Ltd.
3. Mr. Anirudha is working with X & Co. a partnership firm. During the year, the employer firm gifted a diamond ring worth Rs.80,000 to wife of Mr. Anirudha

Solution:

1. Taxable perquisite in the hands of Shradha shall be Rs.10,000 (being Rs.3,000 + Rs.12,000 – Rs.5,000)
2. Taxable perquisite in the hands of Rakhi shall be Rs.11,000.
3. Taxable perquisite in the hands of Mr. Anirudha shall be Rs.75,000.

Question 18:

Find taxable amount of perquisite in the following cases :

1. Y has been allowed a fixed medical allowance of Rs.2,000 p.m.
2. Apart from reimbursement of petty medical bill of Rs.25,000, Z and his family get medical treatment in a dispensary maintained by the employer. Value of facility provided to Z and his family members during the previous year are as follows :

| Particulars | Amount |
|------------------------------------|--------|
| a. Z | 2,000 |
| b. Mrs. Z | 5,000 |
| c. Major son of Z (independent) | 8,000 |
| d. Minor daughter of Z | 25,000 |
| e. Dependent younger brother of Z | 8,000 |
| f. Independent younger sister of Z | 10,000 |
| g. Dependent sister-in-law | 5,000 |

Solution:

1. Medical allowance is fully taxable, hence the taxable amount is Rs.24,000
2. Taxable perquisite in hands of Mr. Z is as under :

| Particulars | Amount |
|------------------------------------|---------------|
| a. Z | Nil |
| b. Mrs. Z | Nil |
| c. Major son of Z (independent) | Nil |
| d. Minor daughter of Z | Nil |
| e. Dependent younger brother of Z | Nil |
| f. Independent younger sister of Z | 10,000 |
| g. Dependent sister-in-law | 5,000 |
| h. Reimbursement of medical bill | 25,000 |
| Taxable Perquisite | 40,000 |

Question 19: Himalaya Ltd. reimburses the following expenditure on medical treatment of the son of an employee Karan. The treatment was done at UK :

1. Travelling expenses Rs.1,15,000.
2. Stay expenses at UK permitted by RBI Rs.45,000 (Actual expenses Rs.70,000).
3. Medical expenses permitted by RBI Rs.50,000 (Actual expenses Rs.70,000).

Compute the taxable perquisites for the assessment year 2023-24 in the hands of Karan, if his annual income from salary before considering medical facility perquisite was (i) Rs.1,50,000; (ii) Rs.2,00,000.

Solution:

Taxable value of perquisite in hands of Mr. Karan is as under :

| Particulars | Workings | Details | Case 1 | Case 2 |
|---------------------|---|-------------------------|------------|------------|
| Medical expenditure | Amount paid in excess of RBI permission and actual expenditure shall not qualify for exemption. | Rs. 70,000 – Rs. 50,000 | Rs. 20,000 | Rs. 20,000 |

| | | | | |
|---------------------------------|---|-------------------------|-------------------|---------------------|
| Stay cost | Stay cost in excess of RBI permission and actual expenditure shall not qualify for exemption. | Rs. 70,000 – Rs. 45,000 | Rs. 25,000 | Rs. 25,000 |
| Travel cost | Travel cost (Note) | | Nil | Rs. 1,15,000 |
| Total taxable perquisite | | | Rs. 45,000 | Rs. 1,60,000 |

Note : Travel cost shall be eligible for exemption only if gross total income of the assessee does not exceed Rs.2,00,000, which can be evaluated as under :

| Particulars | Case 1 | Case 2 |
|---|----------|----------|
| Salaries | | |
| Annual income from salary other than foreign medical perquisites | 1,50,000 | 2,00,000 |
| Add : Medical facility | | |
| Medical expenditure perquisite | 20,000 | 20,000 |
| Stay cost perquisite | 25,000 | 25,000 |
| Gross Total Income for the purpose of foreign travel medical facility | 1,95,000 | 2,45,000 |

Question 20: Following are the particulars of income of Mrs. S. Choudhury for the Previous Year 2022-23:

- Basic salary @ Rs.15,000 per month.
- Dearness Allowance @ 60% of salary.
- Medical Allowance @ 600 per month (Actual expenditure Rs.5,000).
- House Rent Allowance received @ Rs.6,000 per month and she pays rent of Rs.7,200 per month for her house in Durgapur.
- City compensatory allowance Rs.1,500 per month.
- She owns a car which she is using for official purposes. Her employer reimburses her @ Rs.3,000 per month.
- She is contributing Rs.2,100 per month towards a recognized provident fund. The employer is also contributing the same amount. Interest credited to R.P.F @ 11% Rs.2,200.
- She paid Rs.1,800 as professional tax during the year.

Compute income from salary of Mrs. Choudhury for the assessment year 2023-24.

Solution:

Computation of Taxable Salary of Mrs. S Choudhury for the A.Y.2023-24 :

| Particulars | Working | Details | Amount | Amount |
|-----------------------------|--------------|---------|----------|----------|
| Salaries | | | | |
| Basic | | | | 1,80,000 |
| Allowances | | | | |
| Dearness allowance | 60% of basic | | 1,08,000 | |
| Medical Allowance | | | 7,200 | |
| City compensatory allowance | | | 18,000 | |
| House rent allowance | | 72,000 | | |
| Less : Exempted u/s 10(13A) | | | | |

| | | | | |
|---------------------------------|---------------------|--------|--------|-----------------|
| Minimum of the following : | | | | |
| a. Actual HRA | 72,000 | | | |
| b. 40% of (Basic + DA) | 1,15,200 | | | |
| c. Rent paid – 10% (Basic + DA) | 57,600 | 57,600 | 14,400 | 1,47,600 |
| Perquisites u/s 17(2): | | | | |
| Car facility | | | - | - |
| Employer's contribution to RPF | | 25,200 | | |
| Less : Exempted u/s 10(12) | 12% of (Basic + DA) | 25,200 | | |
| Interest on RPF | | 2,200 | | |
| Less : Exempted | Upto 9% | 1,800 | 400 | 400 |
| Gross taxable salary | | | | 3,27,600 |
| Less : Deduction u/s | | | | |
| 16(ia) Standard Deduction | | | 50,000 | |
| 16(iii) Professional tax | | | 1,800 | 51,800 |
| Taxable Salary | | | | 2,75,800 |

PROFITS IN LIEU OF SALARY, GRATUITY, EARNED LEAVE SALARY, PENSION, LEAVE TRAVEL

CONCESSION AND VRS COMPENSATION

Profits in lieu of salary [Section 17(3): "Profits in lieu of salary" includes —

- (1) 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) Any payment due to or received by an assessee from an employer or from a provident fund or other fund, to the extent it does not consist of contributions by the assessee or interest on such contributions.
- (3) Any sum received under a Keyman insurance policy including the sum allocated by way of bonus on such policy.
- (4) 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.

For example: Dearness allowance, house rent allowance, city compensatory allowance, etc. are taxable as profits in lieu of salary.

Exemption available in respect of "Gratuity".

Ans: Gratuity [Section 10(10)]: The exemption to the assessee who are in receipt of gratuity from their employers at the time of death or retirement from employment is as under —

| Section | Particulars of employee | Amount of exemption |
|------------------|---|---------------------|
| 10(10)(i) | Central Government Employees/ Members of civil services/ Local authority employees etc. | Fully exempt |

| | | |
|--------------------|--|--|
| 10(10)(ii) | Other Employees: Employees covered under Payment of Gratuity Act, 1972 | <p>Least of the following is exempt —</p> <p>(i) Rs.20 lakh; or</p> <p>(ii) Actual gratuity received; or</p> <p>(iii) $(15 \div 26) \times \text{Salary last drawn} \times \text{No. of completed years of service or part thereof in excess of 6 months.}$</p> <p>Salary = Basic pay + Dearness allowance (always included).</p> <p>In case of seasonal establishment, 15 days shall be substituted by 7 days.</p> <p>Part of a year exceeding 6 months is taken as a full year.</p> |
| 10(10)(iii) | Employees not covered by the payment of gratuity act ,1972 | <p>Least of the following is exempt —</p> <p>(i) Rs.20 lakh, being the specified limit; or</p> <p>(ii) Actual gratuity received; or</p> <p>(iii) $1/2 \times \text{Average Salary} \times \text{Completed years of service (fraction of a year not to be considered)}$</p> <p>Average salary = Average of salary in last 10 months preceding the month of retirement. For example: Retirement is on 15th February 2022, then average salary will be average of salary from 14th April 2021 to 31 January 2022.</p> <p>Salary = Basic pay + Dearness allowance (to the extent it forms part of retirement benefits) + % wise fixed commission on turnover.</p> |

Notes:

- (1)** Gratuity received by an employee while in employment is fully taxable.
- (2)** If an individual receives gratuity from more than one employer in the same previous year, then the total amount of exemption claimed in that previous year shall not exceed **Rs.20 lakhs**.
- (3)** If an assessee has already availed exemption in respect of any gratuity received from previous employer in earlier years, then while computing the exemption in the current year, the maximum exemption limit of **Rs.20 lakhs** shall be reduced by the amount of exemption already availed.
- (4)** In case if the employee has rendered services to any other employer in the earlier years and did not receive any gratuity from him, then such period of services rendered to his former employer shall also be included while calculating 'completed years of service. **CIT v.PN Mehra (1993) 201 ITR930 (Bom)**

Question 21: Mr Raj is an employee of XYZ Ltd. He received Rs.25,00,000 as gratuity. He retired on 16th February 2023 after rendering 25 years and 7 months of service. His basic salary w.e.f 01-10-2022 was Rs.60,000 per month (prior to that Rs.50,000 p.m). His dearness allowance was Rs.3,11,800 p.m. Calculate the amount of gratuity exempt from tax if

- (i) Mr. Raj is a government employee.
(ii) Mr. Raj is covered by the Payment of Gratuity Act 1972;
(iii) Mr Raj is not covered by the Payment of Gratuity Act, 1972, (40% of dearness allowance form part of salary-for retirement benefits)

Solution: Computation of taxable gratuity shall be as under —

(i) **If Mr. Raj is a Government Employee:** The whole of the gratuity shall be exempt from tax.

(ii) **If Mr. Raj is covered by Payment of Gratuity Act:** The amount of exemption shall be (amounts in

| | |
|--|------------------|
| Completed years of service (Part thereof in excess of 6 months shall be rounded off to higher side.) | 26 |
| Exemption u/s 10(10): Least of the following is exempt | |
| (a) Gratuity received | 25,00,000 |
| (b) $15/26 \times$ Salary last drawn \times Completed years of service (Salary last Drawn = Basic + DA (fully included) = Rs.60,000 + Rs.30,800 = Rs.90,800) | 13,62,000 |
| (c) specified limit | 20,00,000 |
| Taxable gratuity = gratuity received - exemption | 11,38,000 |

(iii) If Mr. Raj is not covered by the Payment of Gratuity Act: The amount of exemption shall be

(amount in Rs.)-

| | |
|--|------------------|
| Gratuity received | 25,00,000 |
| Exemption u/s 10(10): Least of the following is exempt- | |
| (a) Gratuity received | 25,00,000 |
| (b) $\frac{1}{2} \times$ Average Salary (Rs.66,320) \times Completed Years (25) [WN] | 8,29,000 |
| (c) Specified limit | 20,00,000 |
| Taxable gratuity = gratuity received - exemption | 16,71,000 |

Working notes:

| | |
|---|--------------------------|
| Ten months immediately preceding the month of retirement | 01-04-2021 to 31-10-2022 |
| Basic Salary for the said ten months [Rs.50,000 \times 6 + Rs.60,000 \times 4] | 5,40,000 |
| DA (to the extent it forms part of retirement benefits), 40% of Rs.30,800 \times 10 | 1,23,200 |
| total Salary during the said ten months | 6,63,200 |
| Average salary for the said ten months | 66,320 |
| Completed years of service ignoring any fraction | 25 |

Question 22: Compute taxable gratuity: Mr. Shah, an Accounts Manager, has retired from JK Ltd. On 15-1-2023 after rendering services for 30 years 7 months. His salary is Rs.25,000 p.m upto 30-09-2022 and Rs.27,000 thereafter. He also gets Rs.2,000 p.m as dearness allowance (55% of it is a part of salary for computing retirement benefits). He is not covered by the Payments of Gratuity Act, 1972. He has received Rs. 8 lacs as gratuity from the employer company. Compute taxable gratuity. **[4 Marks, IPCC Nov. 2010]**

Solution: Computation of taxable gratuity: The relevant computations are as follows (amount in Rs.)

| | | |
|--|-----------|-----------------|
| Gratuity received | | 8,00,000 |
| Exemption u/s 10(10): The least of the following is exempt | | |
| (a) Gratuity received | 8,00,000 | |
| (b) $1/2 \times \text{Average Salary (26,700)} \times \text{Completed years (30) EWN}$ | 4,00,500 | |
| (c) specified limit | 20,00,000 | 4,00,500 |
| Taxable gratuity=gratuity received-exemption | | 3,99,500 |

Working notes

| | |
|---|------------------------|
| Ten months immediately preceding the month of retirement | 1-3-2022 to 31-12-2022 |
| Basic Salary for the said ten months | 2,56,000 |
| DA (to the extent it forms of retirement benefits, 55% of 2,000 x 10) | 11,000 |
| Total Salary during the said ten months | 2,67,000 |
| Average salary for the said ten months | 26,700 |
| Completed years of service ignoring any fraction | 30 |

Exemption available to assesseees in respect of leave encashment received by them from their employer.

Exemption for leave encashment received by an individual from his employer, on retirement, superannuation or otherwise is as under —

- (i) **In case of Government employees:** Wholly exempt.
- (ii) **In case of any other Employees (including the employees of a local authority! a statutory corporation):** Least of the following is exempt -
 - (a) Actual amount received; or
 - (b) Rs.3,00,000; or
 - (c) 10 months average salary; or
 - (d) Average salary x leaves at the credit of an employee taking 30 days in a year for completed years of service (fraction of year is to be ignored while computing completed years of service)

Where -

- **Salary** = Basic pay + Dearness Allowance (if it forms part of retirement benefits) + Percentage-wise fixed commission on turnover.
- **Average Salary** = Average of salary drawn in the last 10 months immediately preceding the date of retirement. (E.g. - If a person retires on 16th March, 2022, then 10 months average salary shall be computed from 16th May, 2021 to 15 March, 2022)
- **Leaves standing at the credit of employee** = [Annual Leave Entitlement (taking 30 days in a year) x Completed years of actual service rendered] — Leaves actually availed in service.

Other Notes:

- (1) Exemption is also available for leave encashment received on resignation as it is covered under the expression 'otherwise'.
- (2) No exemption is available in respect of leave encashment received during continuity of employment. However, relief u/s 89 can be availed.

- (3) When leave encashment is received by an employee from more than one employer in the same previous year, then the aggregate quantum of exemption must not exceed the limit of Rs.3,00,000 in that year.
- (4) If the employee has already availed an exemption under section 10(10AA) in any earlier year, then the limit of Rs.3,00,000 shall be reduced by the amount of the exemption already claimed for computing the exemption in the current year.
- (5) Leave salary paid to widow/legal heirs of the assessee, who dies during the employment, will not be taxable.
- (6) Leave salary received by the family of government employee or legal heirs of deceased employee is also not taxable in their hands.

Question 23: Computation of taxable earned leave salary: Mr. Bansal was employed in M/s. ABC & Associates. After completing 40 years and 7 months of service he retired on 31st October 2022. From the following information, compute the amount of taxable leave salary -

Salary at the time of retirement – Rs.10,000 p.m.

Average monthly salary for 10 months ending on 31st October 2022 – Rs.9,500 p.m.

Leave entitlement – 1.5 months for each completed year of service.

Leave encashment received on the basis of salary at the time of retirement —Rs. 5,00,000

Solution: The relevant computations are (amount in Rs.) -

| | | |
|--|----------|-----------------|
| Leave salary received | | 5,00,000 |
| Exemption Least of the following is exempt - | | |
| ➤ Actual earned leave salary received | 5,00,000 | |
| ➤ 10 months' Average salary | 95,000 | |
| ➤ Earned leave to the credit x Average Salary (30xRs. 9,500) | 2,85,000 | |
| ➤ Amount notified by the Central Government | 3,00,000 | 95,000 |
| Taxable leave encashment=sum received -exemption | | 4,05,000 |

Working Note: Computation of leave at the credit of an employee:

| Particulars | As per company rules | As per income tax rules |
|---|----------------------|-------------------------|
| Leave entitlement for completed year | 1.5 months | 1 month |
| Completed years of service | 40 | 40 |
| Total leave entitlement (months) | 60 | 40 |
| Leave availed while in service (months) | 10 | 10 |
| Balance leave at his credit (months) | 50 | 30 |

Exemption in respect of Commuted pension.Sec 10(10)

The exemption in respect of commuted pension received by an employee during a previous year is as under

| Particulars of employee | Amount of exemption |
|--|---------------------|
| (1) Employees of the Central Government/ local authorities Statutory Corporation/Members of the Defence Services | Wholly exempt |

| | |
|--------------------------------|--|
| (2) Other employees — | |
| (a) In receipt of gratuity | Exemption=1/3 rd of commuted value of pension |
| (b) Not in receipt of gratuity | Exemption=1/2 of commuted value of pension |

Notes:

- (1) Commuted value of pension = Pension received ÷ % of pension commuted.
- (2) Uncommuted pension is fully taxable for all kinds of employees. (i.e. whether government employee or non-government employee)
- (3) Pension received from UNO is exempt.
- (4) Commuted Pension received from pension fund established by LIC or any other approved insurer under section 10(23AAB) is exempt from tax for all employees.
- (5) Family pension received by legal heirs is not income from salaries, it shall be taxed as 'Income from other sources'.

Question 24: Computation of taxable pension: Rani is entitled to get a pension of Rs.1500 p.m. from Raja Ltd. She gets three-fifth of the pension commuted and receives Rs.90,000. Compute the taxable portion of commuted ,value of pension when

- (i) she does not receive gratuity,
- (ii) receives Rs.50,000 as gratuity.

Solution: Computation of taxable pension

(i) When Rani doesn't receive gratuity:

- (a) % of pension commuted= 3/5= 60%.
- (b) Commuted value of pension (Pension received ÷ % commuted) =Rs.90,000 ÷ 60% = Rs.1,50,000.
- (c) Exemption ½ of commuted value of pension (Rs.1,50,000)= Rs. 75,000
- (d) Taxable portion of commuted pension Rs.90,000 - Rs.75,000 = Rs.15,000.

(ii) When Rani receives gratuity:

- (a) Exemption =1/3rd of commuted value of pension (Rs.1,50,000) = Rs.50,000
- (b) Taxable portion of commuted pension Rs.90,000 — Rs.50,000 = Rs.40,000.

Treatment of Leave Travel Concession (LTC) granted by an employer to his employee.

(1) **Leave Travel Concession [Section 10(5)]:** Section10(5) gives the exemption to an assessee in respect of Leave Travel Concession (LTC) received by or due to him, from his current or former employer, for himself and his family, in connection with his proceedings on leave to any place in India either during his employment or after the retirement/ termination of his employment.

"Family" means, —

- (a) the spouse and children of the individual; and
- (b) the parents, brothers and sisters of the individual or any of them, wholly or mainly dependent on the individual. In case of children born after 1-10-1998, the exemption is available for only two surviving children and in case of birth of multiple children after one child, the multiple children shall be regarded as one child.

(2) **Amount of Exemption [Rule 2B]:**

| Situations | Exemption upto the amount not exceeding** |
|----------------|---|
| Journey by air | Economy fare of national carrier by shortest route. |

| | |
|---|--|
| In case places are connected by rail and journey is performed other than by air | 1 st Class AC rail fare by the shortest route. |
| If places are not connected by rail and — (a) recognised transport system exists (b) no recognised transport carrier exists | 1 st deluxe class fare on such transport by shortest route. 1 st Class AC rail fare by the shortest route (as if the journey had been performed by rail). |
| **The amount of exemption shall not exceed the amount actually incurred for such travel. | |

(3) Claim of Exemption:

(a) The assessee can claim exemption for any two journeys in a block of 4 calendar years.

(b) The current blocks are: Ninth block 2018-2021.

(c) Carry-over of Concession: In case no concession or only one concession is availed in the previous block, then the assessee can claim one additional exemption in the first year of next block.

Question 25: Exemption in respect of leave travel concession u/s 10(5): Mr. Amit avails the benefit of LTC and went by air (economy class) on a holiday in India on 25-01-2023 along with his wife and three children consisting of son aged 6 years and twin daughters of 2 years age. Total cost of tickets reimbursed by his employer was Rs.1,00,000 (Rs.55,000 for 2 adults and Rs.45,000 for the three children). State with reasons the amount which is exempt in the hands of Mr. Amit out of the reimbursement received by him. **(Similar 4 Marks, IPCC May 2013) (Similar: 4 Marks, Nov. 2016)**

What will be your answer in case among his three children, the twins were 6 years old and the age of the son was 2 years?

Solution: Exemption is available under section 10(5) to an employee in respect of value of LTC for himself and his family, in connection with his proceedings on leave to any place in India.

“Family” includes the spouse and children of the individual, In case of children born after 1-10-1998 exemption is available for 2 surviving children. However, exemption shall be available in respect of children born before 1-10-1998 and also in respect of multiple births after one child.

Further, as per Rule 28, if journey is performed by air, the exemption will be available only upto the extent of economy air fare of national carrier by shortest route.

Case I: Son aged 6 years & Twin daughters of 2 years age: This is a case of multiple birth (twin daughters) after one child, hence, all the three children will be eligible for exemption. Accordingly, the whole of the LTC of Rs.1,00,000 will be exempt as the travel is economy class of air.

Case II: twin daughters of 6 years age & son aged 2 years: In this case the number of children is three and one son was born after the multiple birth. Hence, the exemption will be available only in respect of two children and the economy air fare of one child will be taxable. Therefore, taxable value = 45,000 ÷ 3 = Rs.15,000; and the balance of Rs.85,000 will be exempt.

Exemption in respect of Retrenchment Compensation [Section 10(10B)]:

Retrenchment Compensation received by an assessee shall be exempt to the extent of least of the following

- (i)** Actual amount received; or
- (ii)** Rs.5,00,000; or

(iii) An amount calculated in accordance with Section 25F(b) of the industrial Disputes Act, 1947 i.e. 15 days average pay x Every completed year of service or part thereof in excess of 6 months.

Notes:

(1) The above limits will not be applicable to cases where the compensation is paid under any scheme approved by the Central Government for giving special protection to workmen under certain circumstances.

(2) "Average pay" means average of the wages payable to a workman

- in the case of monthly paid workman, in the 3 complete calendar months,
- in the case of weekly paid workman in the 4 calendar weeks,
- in the case of daily paid workman, in the 12 full working days,

preceding the date on which the average pay becomes payable if the workman had worked for 3 complete calendar months or 4 complete weeks or 12 full working days, as the case may be, and where such calculation cannot be made, the average pay shall be calculated as the average of the wages payable to a workman during the period he actually worked.

Question 26: Retrenchment Compensation: Mr. Gobind received retrenchment compensation of Rs.10,00,000 30 years 4 months of service .at the time of retrenchment, he was receiving basic salary of Rs.20,000 p.m dearness allowance of Rs.5000 p.m. compute his taxable retrenchment compensation.(4 marks ,IPCC may 2013)

Solution: Computation of taxable retrenchment compensation (amount in Rs.)-

| | |
|--|------------------------|
| Retrenchment compensation received | 10,00,000 |
| Less: Exemption under section 10(10B) [WN] | <u>4,32,692</u> |
| Taxable retrenchment compensation | <u>5,67,308</u> |

Working Note: Exemption is to the extent of least of the following

- (i) Compensation actually received: Rs.10,00,000
- (ii) Statutory Limit: Rs. 5,00,000 amount calculated in accordance with provisions of the industrial disputes act 1947 i.e.15/26 x avg salary of last 3 months x completed year of service and part thereof in excess of 6months =15/26 x (Rs.20,000 x 3) + (Rs.5,000 x 3)/3x30 years=Rs. 4,32,692.

Exemption in respect of compensation received on voluntary retirement or separation [Section 10(10C)]: Section 10(10C) grants exemption to the employees who are in receipt of voluntary retirement receipts, subject to some conditions -

(1) **Eligible Employees:** Only the employees of following undertakings are eligible —

- (a) A public sector company;
- (b) Any other company;
- (c) An authority established under a Central/State or Provincial Act;
- (d) A local authority;
- (e) A co-operative society;
- (f) A University established or incorporated under a Central/State or Provincial Act and an institute declared to be a University by University Grants Commission;

- (g) An Indian Institute of Technology;
- (h) institute of management as the Central Government may specify in this behalf through a notification in the Official Gazette;
- (i) Central or State Government; or
- (j) An institution having importance throughout India or in any state as the Central Government may specify by notification in the Official Gazette.

(2) Limit of Exemption: Least of the following is **exempt** -

- (a) Actual amount received;
- (b) Rs.5,00,000

The exemption shall be given even if the compensation is receivable in instalments.

(3) Guidelines for claiming exemption [Rule 2BA]:

- (a) the scheme applies to an employee who has completed 10 years of service or completed 40 years of age except in case of employees of public sector company;
- (b) it applies to all employees including workers and executives except directors of a company or co-operative society;
- (c) scheme has been drawn to result in overall reduction in the existing strength of the employees;
- (d) the vacancy caused by the voluntary retirement or voluntary separation is not to be filled up;
- (e) Retiring employee is not employed in another company! concern belonging to same management;
- (f) Amount of compensation does not exceed —
 - (i) 3 months x salary last drawn x completed year of service; or
 - (ii) Salary last drawn x Balance of months left before retirement or superannuation.

Salary = Basic pay + DA (forming part of retirement benefits) + %-wise fixed commission on turnover.

(4) Exemption only once: if exemption has been allowed to an employee under this section in any assessment year, no exemption shall be allowed to him in relation to any other assessment year.

(5) No exemption if relief availed u/s 89: Where any relief has been allowed to an assessee under section 89 for any assessment year in respect of any amount received or receivable on his voluntary retirement or termination of service or voluntary separation, no exemption under this section shall be allowed to him in relation to such, or any other, assessment year.

Thus, relief under section 89 and exemption under this section cannot be availed of simultaneously. Further, once relief is claimed under section 89, the right to claim exemption in respect of VRS compensation is lost forever.

Question 26: VRS compensation-: R is employed in a public company and is-paid a sum of Rs. 6,00,000 on Voluntary Retirement from service. The normal age of retirement in the company is 60 years and R who was 45 years at the time of retirement had completed 20 years of service. His monthly salary at the time of retirement was as follows

| | |
|--|--------|
| Basic Pay | 10,000 |
| Dearness Allowance (50% is includible for pension) | 6,000 |
| HRA | 3,000 |

What is the amount of compensation taxable under the income tax act?

Solution: As per section 10(10C) read with rule 2BA the exemption is available of Rs. 5,00,000 only if the amount received as compensation does not exceed higher of the following limits — amount in

- (a) 3 months x salary last drawn x completed years of service i.e., (3 x Rs.13,000 x 20) [WN] 7,80,000
 - (b) Salary last drawn x No. of months of service left for retirement i.e., (Rs.13,000 x 15 x 12) 23,40,000
- Rs.5,00,000 will be exempt, since the amount received is less than the aforesaid limits, Consequently, 1,00,000 will be taxable.

Working Notes Salary means= Rs. 10,000 + Rs. 3,000 (50% of DA of Rs. 6,000) = Rs.13,000.

Question 27: Computation of taxable compensation: What will be the amount of. Taxable compensation above, if instead of compensation of Rs.6,00,000, R receives a compensation at the time of his retirement of —

- (i) Rs.10,00,000, or
- (ii) Rs.29,80,000.

Solution:

- (i) Here, the amount received is within the limit of Rs.23,40,000, therefore, the exemption under section 10(10C) will be available. The amount taxable at the time of retirement = Rs.10,00,000 — Rs.5,00,000 = Rs. 5,00,000.
- (ii) Since the compensation received exceeds Rs.23,40,000, the payment is not in accordance with Rule 2BA and therefore no exemption will be available under section 10(10C). 'therefore, entire compensation will be taxable i.e. Rs.29,80,000.

Exemption in respect of tax on non-monetary perquisites borne by the employer on behalf of employee [Section 10(10CC)]:

This section provides the exemption to an employee in respect of the tax paid by his employer on his behalf on the non-monetary perquisites [within the scope of Section 17(2)] received by such employee. Hence, such tax paid shall not form part of the employee's gross salary.

Tax implication in hands of employer: Section 40(a)(v) disallows such expenditure in the hands of the employer. Therefore, the tax so paid by the employer will not be deductible expenditure in his hands.

TAX TREATMENT OF PROVIDENT FUND AND TAX RELIEF

Tax implications in respect of Various Provident Funds.

(1) Provident fund scheme In a Provident Fund Scheme, employer deducts a certain amount from the salary of employee for the purpose of contribution towards a fund and the employer also contributes to the same. Both the contributions are invested in securities and interest earned thereon is credited to the fund.

Hence, Provident Fund consists of-

- (a) employer's contribution and interest thereon; and
- (b) employee's contribution and interest thereon.

(2) The various provident funds are -

- (a) **Statutory Provident Fund (SPF)** Statutory provident fund is set up under the provisions of the Provident Funds Act, 1925. This fund is maintained by Government and semi-Government organizations, local authorities, railways, universities and recognised educational institutions.

(b) Recognised Provident Fund (RPF). A provident fund scheme to which the Employee's Provident Fund and Miscellaneous Provisions Act, 1952 applies is Recognised Provident Fund. Besides, these funds are recognized by the Principal CIT or CIT or Principal CCIT or CCIT under the provisions of the Income Tax Act, 1961. The Principal CIT or CIT recognizes only those funds which follow the rules given in the Fourth Schedule of income-tax Act.

(c) Unrecognised Provident Fund (URPF): if a provident fund is not recognized by the Principal CIT or CIT of Income tax, it is known as unrecognized provident fund,

(3) Tax treatment of various Provident Funds:

| Tax incidence of | SPF | RPF | URPF |
|---|-------------------|--|--|
| (1) Employers contribution | Exempt | Exempt upto 12%of salary [note 1 & 2] | Not taxable when the contribution is made |
| (2) Employee contribution | taxable | taxable | taxable |
| (3) Deduction u/s 80C on employee's contribution | Available | Available | Not available |
| (4) Interest credited to PF | Exempt | Exempt upto interest calculated @ 9.5% p.a. [Note-3&6] | Not taxable when the interest is credited |
| (5) lump sum payment at the time of retirement or termination of service | Exempt u/s 10(11) | Exempt from tax in some cases. When not exempt provident fund will be treated as an unrecognised fund from the beginning. [Note-4J] | <ul style="list-style-type: none"> ➤ Employer's contribution & interest thereon: Taxable as salary. Relief can be claimed u/s 89. ➤ Employee's own contribution: Exempt, as taxed earlier. ➤ Interest on employees contribution: Taxable as 'income from other sources' |

Note:

(1) Salary= Basic + Dearness allowance, if the terms of employment so provide + percentage-wise fixed commission on turnover.

(2) The amount or the aggregate of amounts of any contribution made to the account of the assessee by the employer —

(a) in a recognised provident fund;

(b) in the scheme referred to in Section SOCCD(1); and

(c) in an approved superannuation fund,
to the extent it does not exceed Rs. 7,50,000 in a previous year is exempt from tax.

- (3) The annual accretion by way of interest, dividend or any other amount of similar nature during the previous year to the balance at the credit of the fund or scheme referred above to the extent it relates to the contribution which is included in total income in any previous year computed in such manner as may be prescribed.

The CBDT has, vide Rule 3B, notified the following manner to compute the annual accretion by way of interest, dividend or any other amount of similar nature during the previous year —

$$TP = (PC/2) \times R + (PC1 + TP1) \times R$$

Where,

| | |
|------|--|
| TP | Taxable perquisite under section 17(2)(viiia) for the current previous year |
| PC | Amount or aggregate of amounts of employer's contribution in excess of Rs. 7.5 lakh to recognized provident fund, national pension scheme u/s 80CCD and approved superannuation fund during the previous year |
| PC1 | Amount or aggregate of amounts of employer's contribution in excess of Rs.7.5 lakh to recognized provident fund, national pension scheme u/s 80CCD and approved superannuation fund for the previous year or years commencing on or after 1 April, 2020 other than the current previous year |
| TPI | Aggregate of taxable perquisite under section 17(2)(viiia) for the previous year or years commencing on or after 1 April, 2020 other than the current previous year |
| R | I/Favg |
| I | Amount or aggregate of amounts of income accrued during the current previous year in recognized provident fund, national pension scheme u/s 80CCD and approved superannuation fund |
| Favg | (Amount or aggregate of amounts of balance to the credit of recognized provident fund, national pension scheme u/s 80CCD and approved superannuation fund on 1st April, 2021 + Amount or aggregate of amounts of balance to the credit of recognized provident fund, national pension scheme u/s 80CCD and approved superannuation fund on 31st March, 2022)/2 |

Where the amount or aggregate of amounts of TPI and PCI exceeds the amount or aggregate of amounts of balance to the credit of the specified fund or scheme on 1ST April, 2021, then, the amount in excess of the amount or aggregate of amounts of the said balance shall be ignored for the purpose of computing the amount or aggregate of amounts of TP1 and PC1.

- (4) Lump sum payment at the time of retirement or termination of service is exempt from tax if:
- (a) the employee has rendered continuous service with his employer for a period of 5 years or more.
 - (b) Service is terminated due to ill health of employee or discontinuance of employer's business or any other reason beyond his control; or

- (c) On cessation of employment, he takes employment with another employer, exemption is allowed to the extent such accumulated balance transferred to his RPF account maintained by other employer; or
 - (d) The entire balance standing to the credit of the employee is transferred to his account under a pension scheme referred to the previous section 80CCD) and notified by the Central Government.
- (5) In case if the employee has transferred his PF balance with the previous employer to the PP a/c maintained with the current employer, then for determining the period of 5 years, services rendered to the previous employer shall also be considered.
- (6) **Taxability of accrued interest from SPF/RPF [Amended by Finance Act, 2021 w.e.f. 1-4-2022 i.e. AY 2022-23]:** 'Exemption U/S 10(11)/10(12) shall not apply to the income by way of interest accrued during the previous year in the account of a person to the extent it relates to the amount or the aggregate of amounts of contribution made by that person exceeding Rs.2,50,000(Rs.5,00,000 if no contribution by the employer of such person) in my previous year in that fund, on or after 1-4-2021 and computed in such manner as may be prescribed.
- It may be noted that interest accrued on contribution to such funds upto 31-03-2021 would be exempt without any limit, even if the accrual of income is after that date.
- (7) **Tax liability on transfer from URPF to REF:** In case if URPP is converted into RPF, then the amount to be taxed shall be the amount which is arrived by treating the fund as RPF from its inception i.e. from the year of creation of fund.

Tax incidence of approved superannuation funds.

The tax treatment of approved superannuation funds is as follows -.

- (1) **Employer's contribution to the fund** — Exempt if the amount or the aggregate of amounts of any contribution made to the account of the assessee by the employer in a RPP, NPS scheme and in an approved superannuation fund, to the extent it does not exceed Rs.7,50,000 in a previous year.
- (2) **Employee's contribution** - qualifies for deduction under section 8f1C.
- (3) **Interest credited to the employee's account** — **Exempt.** However, the annual accretion by way of interest, dividend or any other amount of similar nature during the previous year to the balance at the credit of the fund or scheme referred above to the extent it relates to the contribution which is included in total income in any previous year computed in such manner as may be prescribed.
- (4) **Exemption of payment from the fund [Section 10(13)]:** Section 10(13) gives exemption in respect of payments from an approved superannuation fund if they are made,
 - (a) to legal heirs on the death of the beneficiary; or
 - (b) to an employee in substitution of or in commutation of an annuity on his retirement at or after a specified age or if he becomes incapable prior to his retirement; or
 - (c) in form of refund of contribution on death of beneficiary; or
 - (d) in the form of refund of contribution to an employee leaving the service in circumstances other than those mentioned in (c) above, to the extent the payment does not exceed contribution made prior to commencement of this Act and interest thereon; or
 - (e) by way of transfer to the account of the employee under a pension scheme referred to in section 80CCD and notified by the Central Government.

Question 28: Computation of taxable salary: Mr. M is an area manager of M/s. N Steels Co. Ltd. During the previous year 2022-23 he gets following emoluments from his employer:

| | |
|---|------------------------------|
| basic salary: upto 31-08-2022 | Rs.20,000 p.m. |
| from 01-09-2022 | Rs.25,000 p.m. |
| Transport Allowance | Rs.2000 p.m |
| Contribution to recognized provident fund 15% of basic salary and D A | 15% of basic salary and DA |
| Children education allowance | Rs.500 p.m, for two children |
| City Compensatory Allowance | Rs.300 p.m |
| Hostel expenses allowance - | RS.380 P.M for two children |
| Tiffin in allowance (actual expenses Rs.3,700) | Rs.5,000 p a |
| Tax paid on employment | Rs.2,500 |

Compute taxable salary of Mr. M. if he has not opted for the provisions of Section 115BAC.

(6 Marks, PCC Nov. 2008)

Solution: Computation of income from salary of Mr. M (amount in Rs.):

| | | |
|---|--------|----------|
| Basic salary (Rs.20,000 x 5 ÷ Rs. 25,000x7) | | 2,75,000 |
| Transport allowance(2000 p.m x12) | 24,000 | |
| Less: exempt | nil | 24,000 |
| Children education allowance (Rs.500 p.m x12) | 6,000 | |
| Less: exempt(Rs.100 x2x12) | 2,400 | 3,600 |
| City compensatory allowance | | 3,600 |
| Hostel expenses allowance(Rs.380x12) | 4,560 | |
| Less: exempt (Rs.300 x 2 x 12)=Rs.7,200 but restricted to the actual allowance of Rs.4560 | 4,560 | Exempt |
| Tiffin allowance(fully taxable) | | 5,000 |
| Tax paid on employment(employee's obligation met by employer)[WN 2] | | 2,500 |
| Employer contribution to R.P.F in excess of 12%of salary(i.e.,3% of Rs.2,75,000) [WN 1] | | 8,250 |
| Gross salary | | 3,21,950 |
| Less: standard deduction u/s 16(ia) [WN 3] | | 50,000 |
| Employment tax u/s section 16(iii) | | 2,500 |
| Taxable salary | | 2,69,450 |

Working Notes:

- (1) The question states that contribution to recognised provident fund is at 15% of Basic salary + D,A. However, since the amount or rate of D.A. is not given in the question, contribution to recognised provident fund has been taken as 15% of basic salary.
- (2) Employment tax paid by employer should be included in the salary of Mr. M as a perquisite since it is discharge of monetary obligation of the employee by the employer. Thereafter, deduction of employment tax paid is allowed to the employee from his gross salary.
- (3) As per Section 16(ia), standard deduction will be allowed from gross salary amounting Rs.50,000 or the amount of salary, whichever is less.

Basic salary (Rs.20,000 x 5 ÷ Rs.25,000 x Rs.2,75,000)

Relief computed when salary is paid in arrears or in advance

The provisions relating to tax relief under Section 89 are as under:

- (A) Relief when available:** Section 89 read with Rule 21A grants relief to the assessee who receives —
- salary, being paid in arrears or in advance; or
 - salary for more than 12 months in any one financial year; or
 - profits in lieu, of salary under section 17(3); or
 - family pension as referred to in Section 57(ia) being paid in arrears,
- due to which his total income is assessed at a rate higher than that at which it should have been assessed.
- (B) Calculation of relief:** The admissible relief will be calculated as per the following steps —
- Calculate the tax payable on the total income, including the additional salary, of the previous year in which the same is received.
 - Calculate the tax payable on the total income, excluding the additional salary of the previous year in which the same is received.
 - Find out the difference between the tax at (1) and (2).
 - Compute tax on total income after including the additional salary in the previous year to which such salary relates.
 - Compute tax on total income after excluding the additional salary in the previous year to which such salary relates
 - Find out the difference between tax at (4) and (5).
 - Relief under section 89 Tax computed at (3) -. Tax computed at (6).
- (C) No relief, if exemption claimed u/s 10(10C) in respect of VRS compensation:** No relief shall be granted under this section in respect of any amount received or receivable by an assessee on his voluntary retirement or termination of his service under Voluntary Retirement or Separation Scheme if an exemption u/s 10(10C) has been claimed in respect of such or any other assessment year.
- Effect:** The cumulative effect of sections 10(10C) and 89 is
- The assessee cannot avail of exemption u/s 10(10C) and simultaneously claim relief u/s 89 in respect of the un-exempt portion in the same assessment year;
 - Once exemption is claimed u/s 10(10C), no exemption u/s 10(10C) and no relief u/s 89 can be claimed for any other assessment year in respect of VRS compensation;
 - Once relief is claimed u/s 89 in respect of VRS compensation received, no exemption u/s 10(10C) can be claimed for any other assessment year. However, if any VRS compensation is received subsequently from any other employer, relief u/s 89 can be claimed. Therefore, relief u/s 89 can be claimed more than once.

Question 29: Ta relief: Mr Ashok Kumar, an employee of a PSU, furnishes the following particulars for the previous year ending 31 3-2023.

| | Particulars | Rs. |
|----|--|----------|
| a) | Salary income (computed) for the year | 8,25,000 |
| b) | Salary for financial year 2009-10 received during the year | 40,000 |
| c) | Assessed income for the financial year 2009-10 | 1,40,000 |

You are requested to compute relief under section 89 of the income tax act 1961, in terms of tax payable

The rates of income tax for the assessment year 2010 - 11 are -

On first Rs.1,00,000 : Nil

On Rs.1,00,000 - Rs.1,50,000 : 10%

On Rs.1,50,000 - Rs.2,50,000 : 20%

Above Rs.2,50,000: 30% education cess @2% of tax payable. (7 marks, modified PCC June 2009)

Solution: Computation of relief under section 89-

| Particulars | Tax liability for 2022-23 | | Tax liability for AY 2010-11 | |
|---|-----------------------------|------------------------|------------------------------|------------------------|
| | Salary inclusive of arrears | Salary without arrears | Salary inclusive of arrears | Salary without arrears |
| | (1) | (2) | (3) | (4) |
| Actual salary | 8,65,000 | 8,25,000 | 1,80,000 | 1,40,000 |
| Income tax thereon | 85,500 | 77,500 | 11,000 | 4,000 |
| HEC @4% EC @2% | 3,420 | 3,100 | 220 | 80 |
| Total tax liability | 88,920 | 80,600 | 11,220 | 4080 |
| Step 1: tax at (1)-tax at(2) | | 8,320 | | |
| Step 2: tax at (3)-tax at(4) | | | | 7,140 |
| Relief u/s 89: step1 - step2 | | 87,740 | | |
| Tax payable [tax (1)-relief](rounded off) | | 87,740 | | |

Assumption: Arrears of salary of financial year 2009-10 are not included in salary income of current year.

THE END

4. INCOME FROM HOUSE PROPERTY

In general where a person living in India he may have his own house or he may live in the property of others, when he is living in others property he have to pay rental. Such rental money is an income to the house owner and it is chargeable in the head of Income.



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The process of computation of income under the head “Income from house property” starts with the determination of annual value of the property. The concept of annual value and the method of determination is laid down in section 23.

Chart of computation of Income from House Property

| Particulars | Let out/Deemed Let out/Self-occupied for a part of year and let out for another part. | Self-occupied property (One/Two) whose annual value is/are assessed at Nil u/s 23(2) |
|--|---|--|
| Gross Annual Value [Section 23(1)] | xxxx | Nil |
| Less: Municipal Taxes actually paid by the assessee during the previous year | xxxx | Nil |
| Net Annual Value (NAV) | xxxx | Nil |
| Less: Deductions under section 24 - | | |
| (a) 30% of NAV | xxxx | Nil |
| (b) Interest on borrowed capital | xxxx | Xxxx |
| | (Actual interest payable without any limit) | (Actual interest up to maximum of Rs.30,000 or Rs.2,00,000) |
| Income from house properly | xxxx | xxxx |

Chargeability of Income from House Property under section 22

Income from House Properly [Section 22]: The annual value of property consisting of any buildings or land appurtenant thereto of which the assessee is the owner, other than such portions of such property as he may occupy for the purposes of any business or profession carried on by him the profits of which are chargeable to tax, shall be chargeable to Income-tax under the head “Income from house-property”.

Conditions to be fulfilled for the purpose of charging any Income under this head:

(1) Property must consist of any building or land appurtenant thereto —

- (a) **Scope of buildings:** Buildings includes residential buildings, factory buildings, offices, shops, etc. Building constructed on leasehold/rented land is also covered here.
- (b) **Rent of vacant land — taxable under ‘Income from Other Sources’:** Income from letting out any vacant land is not taxable as ‘income from. house property’, but taxable as ‘income from other sources’, since vacant land cannot be taken as land appurtenant to a building.

(2) Assessee must be the owner of such property —

- (a) Ownership covers free-hold as well as leasehold rights and deemed ownership under section 27.
- (b) Ownership must exist in the previous year (not necessary to be in assessment year) of which assessment is to be done.

(3) The property can be used for any purpose except for the purpose of business or profession of the assessee —

- (a)** The property can be used for any purpose by the assessee, however it should not be used by him for the business or profession, whose profits are chargeable to tax.

The income earned by an assessee engaged in the business of letting out of properties on rent would be taxable as business income. - **Rayala Corporation (P) Ltd. v. Asstt. CIT 120161386 ITR 500 (SC)**

- (b)** In case property is used by the assessee for his own business, then neither the notional rent of property used shall be allowed as deduction while calculating business income nor the notional income shall be taxed under section 22. (Purpose incidental to business shall be considered as business purpose).

(4) Property held as stock-in-trade etc.: Annual value of house property will be charged under the head “income from house property”, where it is held by the assessee as stock-in-trade of a business also.

However, the annual value of property being held as stock in trade would be treated as Nil, for a period of two years from the end of the financial year in which certificate of completion of construction of the property is obtained from the competent authority, if such property is not let-out during such period. **[Section 23(5)]**

Exceptions:

- (a) Sublet receipts — Taxable under income from Other Sources’:** In case of sub-letting, since the assessee is not the owner of the building sublet, hence the ‘income derived therefrom shall not be taxable as income from house property, but shall be taxable as income from other sources’

- (b) Principle of Mutuality:** When the assessee is governed by principle of mutuality, then the income from property will also be governed by the said principle and hence, not taxable under the head ‘income from House Property’

Example - Annual value of property of a social club will be outside the scope of the levy of income tax

- (c) Letting is incidental to main business’** In case the letting out of property is incidental to the main business, then income from such property shall be taxable as ‘Profits and gains of business profession

Example - An assessee lets out his house property to his employees/directors for efficient conduct of his business, then such property will be considered as being used for the business purpose and hence, taxable as ‘Profits and gains of business or profession’.

- (d) Assessee’s property used for his partnership firm:** In case any property is owned by an assessee and the same is given by him to the partnership firm, in which he is a partner, for carrying on the business of such firm, then it will be treated as if the property is used by the assessee for his own business and thus, the income from such property will not be taxable under this head.

However, if property owned by HUF is given on rent to a firm in which members of HUF are partners in their personal capacity, then the rental income from such property’ shall be taxed as ‘income from house property in the hands of HUF.

Question 1:

State the head of income in the following cases under which the receipt is to be assessed and comment

- (a) A uses his property for his own business Can he claim depreciation’**

- (b) B lets out his property to X, X sublets it. How is sub-letting to be assessed in the hands of X?**

(c) C has built a house on a leasehold land, He has let out the property and claims the rent as income from house property and deducted expenses on repairs, security charges, insurance and collection charges totaling to 40% of receipts,(4 marks, IPCC May 2013)

Ans: The taxability of income under various heads is as under

- (a)** Yes, even if property is used for assessee's own business depreciation is allowed u/s 32 of income tax Act, 1961.
- (b)** Income from sub-letting is taxable under the head income from other sources.
- (c)** Even if property is built on a leasehold land the assessee will be regarded as owner of such house property and rental income will be taxed under Income from house property. However, standard deduction of 30% of net annual value is allowed while computing income from house property. Hence, he will not be entitled deduction on repairs, security charges, insurance and collection charges totaling to 40% of receipts.

Applicability of section 22 for chargeability of income tax for house property with disputed ownership.

Disputed Ownership If the title of ownership of the house property is under dispute in a court of law, the decision about who is the owner lies with the Income tax department. The assessment cannot be held up for such dispute. Generally, a person who receives the income or who enjoys the possession of the house property as owner, though his claim is under dispute, is assessable to tax under section 22.

Tax treatment of composite rent under the income tax Act,1961

Composite Rent The rent received by the owner of a property in respect of building as well as other assets like furniture, plant & machinery etc.; or for different services in the building like lifts, security, etc., is known as Composite Rent.

Tax Treatment of Composite Rent:

(1) Composite Rent including rent for letting out of property as well as rendering of services —

- (i)** Where letting out of property and rendering of services are huge different line of activities or two different sources: To be apportioned as 'property income' and 'business income or income from other sources'.
- (ii)** Where the two activities are related to the extent that they form a single activity for all purposes, then —
 - (a) if the main intention is letting out the property:** It will be taxable under Income from House-Property.
 - (b) if the main intention is to exploit the immovable property by way of complex commercial activities:** It will be taxable under Profits & gains of business or profession.

(2) Composite Rent including rent for letting out of building as well as other assets like plant, machinery, furniture : According to Section 56(2)(iii) —

- (i)** If letting of property is inseparable from letting of other assets: **Entire income is taxable as 'Business income or Income from other sources'.**
- (ii)** If letting of property is separable from letting of other assets: Rent for house is taxable as '**House property income**' and rent for other assets is taxable as '**Business income or income from other sources**'.

COMPUTATION OF ANNUAL VALUE –SECTION 23

Computation of Annual value of a House property

Ans: The annual value of a House Property is computed in the following two steps —

(1) Computation of Gross Annual Value (GAV) as per section 23(1).

(2) Computation of Net Annual Value (NAV).

(1) Computation of Gross Annual Value (GAV) [Section 23(1)] : For the purpose of Section 22, the gross annual value shall be deemed to be —

(a) Expected Rent section 23(1)(a): Expected rent is the sum for which the property might reasonably be expected to be let out from year to year. It is the sum higher of Fair Rent and Municipal Rent (Valuation) but it cannot exceed Standard Rent fixed by any Rent Control Act.

Expected Rent (ER) = Municipal Valuation or Fair Rent, whichever is higher, subject to maximum of Standard Rent.

(b) If Actual Rent Received or Receivable (ARR) exceeds Expected Rent (ER) - ARR to be GAV [Section 23(1)(b)] : Where the property or any part of property is let out and the actual rent received or receivable by the owner is in excess of the sum referred to in (a) above, amount so received or receivable shall be GAV. Gross Annual Value (GAV) = Actual Rent Received or Receivable (ARR), if ARR exceeds ER.

(c) Actual rent received/ receivable (ARR) Is less than Expected Rent (ER) [Section 23(1)(c)]: Where the property or any part of the property is let out and was vacant during the whole or any part of the previous year and owing to such vacancy, the actual rent received or receivable by the owner in respect thereof is less than the sum referred to in (a) above, amount so received or receivable shall be GAV.

Gross Annual Value (GAV) = Actual Rent Received or Receivable (ARR).

(2) Computation of Net Annual Value (NAV): Net Annual Value is the sum arrived at after deducting the taxes levied by any local authority on such property paid by owner, from the Gross Annual Value.

NAV = Gross annual value — Municipal Taxes paid by the owner during the previous year.

Notes:

(A) Treatment of Unrealised Rent: Unrealised Rent shall be deducted from actual rent received or receivable if it is proved to be lost and irrecoverable.

As per Rule 4, the amount of rent which the owner cannot realize (Unrealised Amount) shall be equal to the amount of rent payable but not paid by a tenant of the assessee and so proved to be lost and irrecoverable, where —

(i) the tenancy is bonafide;

(ii) the defaulting tenant has vacated, or steps have been taken to compel him to vacate the property;

(iii) the defaulting tenant is not in occupation of any other property of the assessee; and

(iv) the assessee has taken all reasonable steps to institute legal proceedings for the recovery of the unpaid rent or satisfies the Assessing Officer that legal proceedings would be useless.

(B) Determining whether Actual rent received/receivable is less than Expected rent, due to vacancy or not: Expected rent shall be made proportionate for the period for which property is let out i.e. Proportionate Expected Rent (PER) shall be calculated as follows:

$$\text{PER} = \frac{\text{ER for 12 months} \times \text{Months for which property was let out}}{12}$$

If ARR exceeds PER, it means that the ARR is less than ER due to vacancy and hence, $\text{GAV} = \text{ARR}$.

If ARR is less than PER, it means that the ARR is less than ER not due to vacancy but on account of other factors and hence, $\text{GAV} = \text{ER for 12 months}$.

(C) Deduction of Municipal Taxes: Municipal taxes are allowed as deduction only if they have been actually paid by the assessee himself during the previous year, irrespective of the year to which such taxes relate.

As per Section 27(vi), taxes; levied by a local authority in respect of any property shall be deemed to include service taxes levied by local authority in respect of the property.

Taxes must be paid by assessee; if they have been paid by tenant, no deduction will be allowed.

(D) Vacancy for the whole year: if the property was vacant during the whole of the previous year, then the annual value of such property shall be NIL because in that case ARR shall be NIL and it is less than the ER owing to such vacancy.

Question 2: Computation of Gross annual value : Mr. Vallaba owns five houses at Cochin. Compute the gross annual value of each house from the information given below:

| Particulars | HOUSE - I | HOUSE - II | HOUSE - III | HOUSE - IV | HOUSE - V |
|-----------------------------------|-----------|------------|-------------|------------|-----------|
| Municipal Value | 120000 | 240000 | 110000 | 90000 | 75000 |
| Fair rent | 150000 | 240000 | 114000 | 84000 | 80000 |
| Standard Rent | 108000 | N.A | 144000 | N.A | 78000 |
| Actual Rent Received / Receivable | 180000 | 210000 | 120000 | 108000 | 72000 |

Solution: Computation of Gross Annual Value (amount in Rs.)-

| Particulars | House I | House II | House III | House IV | House V |
|--|---------|----------|-----------|----------|---------|
| Expected Rent [WN] | 108000 | 240000 | 114000 | 90000 | 78000 |
| Actual rent receivable | 180000 | 210000 | 120000 | 108000 | 72000 |
| Gross annual value (Higher of the above two) | 180000 | 240000 | 120000 | 108000 | 78000 |

Working Note: ER = Municipal Value or Fair Rent, whichever is higher subject to maximum of Standard Rent.

Question 3: Computation of Gross Annual Value : Vinodni is the owner of the three houses, which are all let out and covered by the Rent Control Act. From the following particulars, find out the gross annual value in each case:

| Particulars | House - I | House - II | House - III |
|-------------------|-----------|------------|-------------|
| Municipal value | 30000 | 26000 | 35000 |
| Annual rent | 42000 | 36000 | 30000 |
| Fair rent | 36000 | 28000 | 30000 |
| Standard rent | 30000 | 35000 | 36000 |
| Unrealised rent | 7000 | 9000 | 2500 |
| Period of vacancy | 1 Month | 2 Month | 3 Month |

Solution: Computation of Gross Annual Value (amount in Rs.)

| Particulars | House - I | House - II | House - III |
|---|-----------|------------|-------------|
| Expected rent | 30000 | 28000 | 35000 |
| Let out period (in months) [WN-1] | 11 | 10 | 9 |
| Proportionate expected rent for the let out period (PER) [WN-2] | 27500 | 23333 | 26250 |
| Actual rent for let out period | 38500 | 30000 | 22500 |
| Actual rent received (ARR) [WN-3] | 31500 | 21000 | 20000 |
| Gross Annual Value (GAV) [WN-4] | 31500 | 28000 | 35000 |

Working Notes:

- (1) ER Municipal Value or Fair Rent, whichever is higher subject to maximum of Standard Rent.
- (2) $PER = ER \times \text{Let out period} \div 12$.
- (3) $APR = \text{Actual rent} - \text{Unrealised rent}$.
- (4) If ARR is greater than or equal to PER, then $GAV = ARR$, otherwise $GAV = ER$.

Computation of annual value in case of a self-occupied house property.

Self-Occupied Property [Section 23(2)]: Where the property consists of a house or part of a house which —

- (a) is in the occupation of the owner for the purposes of his own residence; or
- (b) 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, he has to reside at that other place in a building not belonging to him i.e. **(unoccupied property)**, the annual value of such house or part of the house shall be taken to be Nil.

The benefit of "Nil" Annual Value is available for two self-occupied or unoccupied house property i.e. for either one house property or two house properties

Notes:

- (i) Since here annual value will be NIL, hence municipal taxes paid have no relevance.
- (ii) The annual value will be NIL only if self-occupied by the owner himself, hence no such benefit of self-occupation is available if occupied by the relatives of the owner.
- (iii) If the assessee has let out his house property to his employer and the employer has allotted the same to the assessee as rent-free quarters, then such house property allotted cannot be considered as self-occupied by the assessee under section 23(2), and hence no benefit shall be available to the assessee.
- (iv) The benefit of "Nil" Annual Value in respect of up to two self-occupied house properties is available only to an individual/ HUF.

Tax treatment of House Property if it is

- (i) **Let out for certain period and self-occupied for the remaining period, or**
 - (ii) **Let out for certain portion and self-occupied for the remaining portion.**
- (1) House property let out for certain period and self-occupied for the remaining period:** As per Section 23(3), the annual value will not be taken as Nil if —
- (a) 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.

Hence, in such case annual value shall be computed as per Section 23(1) i.e. actual rent for let-out period shall be compared with expected rent of 12 months to determine the gross annual value.

(2) House property let out for certain portion and self-occupied for the remaining portion:

- (a) The annual value of let out portion will be computed as per the provisions of Section 23(1) and the value of self-occupied portion as per the provisions of Section 23(2)(a) i.e. the value will be Nil of such self-occupied portion.
- (b) If municipal value or fair rent are not given separately, then they are to be apportioned between the let out portion and self-occupied portion on some reasonable basis, E.g.- plinth area, built-up floor space, etc.

Deemed to be let-out property [Section 23(4)]:

Where more than two houses are self-occupied by the assessee then —

- (i) the provisions of section 23(2) shall apply only in respect of two of such houses, which the assessee may, at his option, specify in this behalf i.e. two houses at option of assessee shall be treated as self-occupied;
- (ii) the annual value of the other house(s) shall be determined u/s 23(1) as if such house(s) had been let-out.

Computation of income from house property which is held by the assessee as stock in trade.

House property held as stock in trade - Notional income not to be taxable up to two years [Section 23(5)]: The annual value of property or part of the property shall be taken as Nil if the following conditions are to be satisfied

- (i) The property must consist of any building or land appurtenant thereto is held as stock-in-trade by the owner of the property.
- (ii) The property or any part of the property is not let during the whole or any part of the previous year. However, the annual value of such property or part of the property shall be taken as NIL only for the period up to two years from the end of the financial year in which the certificate of completion of construction of the property is obtained from the competent authority.

Question 4: Computation of income from House Property: XYZ Ltd. is engaged in construction of residential flats. One building consisting of 25 residential apartments was constructed and completion certificate was obtained on 15-07-2020. Out of 25 residential apartments 5 apartments remained unsold 31-03-2024. The expected rent of each apartment is Rs.30000 per month. You are required to determine Income from House property for the assessment year 2023-24 and assessment Year 2024-25.

Solution: As per provisions of Section 23(5), where the house property consisting of any building and land appurtenant thereto is held as stock-in-trade and the property or any part of the property is not let during the whole or any part of the previous year, the annual value of such property or part of the property, for the period up to two years from the end of the financial year in which the certificate of completion of construction of the property is obtained from the competent authority, shall be taken to be nil.

Thus the income from house property up to 31-03-2023 i.e., two years from end of Financial Year 2020-21 shall be taken as NIL. Thus, income from house property for AY 2023-24 shall be taken as NIL.

Computation of income from House property for Assessment Year 2024-25: (amount in Rs.)

| | |
|--|------------------|
| Expected Rent being Gross annual value (30,000 x 12 x 5) | 18,00,000 |
| Less: Municipal taxes paid | Nil |
| Net Annual Value | 18,00,000 |
| Less: Deductions under section 24 (Statutory deduction @ 30% of NAV) | 5,40,000 |
| INCOME FROM HOUSE PROPERTY | 12,60,000 |

DEDUCTION FROM ANNUAL VALUE –SECTION 24**Deductions under section 24:**

Income chargeable under the head “Income from house property” shall be computed after making the following deductions, namely —

- (a) Statutory deduction :** A sum equal to 30% of annual value;
- (b) Interest on borrowed capital:** Where the property has been acquired, constructed, repaired, renewed or reconstructed with borrowed capital, the amount of any interest payable on such capital.

Pre-construction acquisition period : Where the property has been acquired or constructed with borrowed capital, then the interest payable on such borrowed capital, relating to pre-acquisition or pre-construction period, shall be allowed in 5 equal installments beginning with the previous year in which house is completed and 4 succeeding years. Where -

- (A) Pre-acquisition/pre-construction period shall -**
- (i)** start from the date of borrowing; and
 - (ii)** end on —
 - (a)** 31st March preceding the year of completion of construction or acquisition; or
 - (b)** on the date of actual repayment of loan, whichever is earlier.
- (B) Interest of pre-acquisition or pre-construction period =** Loan taken for acquisition and construction of a house property x Rate of Interest x Pre-acquisition or pre-construction period.

Maximum deduction for interest allowable when the one/two houses are Self-occupied/: The maximum limit is Rs.2,00,000 (for one or two houses in aggregate) with following break-up -

| Case | Amount of deduction |
|---|---|
| <p>(1) Interest on capital borrowed on or after 1-4-1999 for acquisition or construction of house/s.</p> <p>(A) Conditions: This case is applicable only if -</p> <ul style="list-style-type: none"> (i) such acquisition or construction is completed within 5 years from the end of the financial year in which capital was borrowed; and (ii) the assessee furnishes a certificate, from the person to whom any interest is payable on the capital borrowed, specifying the amount of interest payable by the assessee. <p>(B) New loan also covered: Deduction is admissible even If the Interest pertains to a new loan taken by the assessee for repayment of whole or any part of capital borrowed earlier.</p> | <p>Actual interest payable in aggregate for one or two self- occupied properties, subject to maximum of Rs.2,00,000</p> |

| | |
|---|---|
| <p>(2) In any other case i.e. If the interest relates to</p> <p>(A) Capital borrowed before 1-4-1999 for acquisition, construction, repair renewal or reconstruction of house property; or</p> <p>(B) Capital borrowed on or after 1-4-1999 for repair, renewal or reconstruction of house; or</p> <p>(C) Capital borrowed as per (1) above but any condition mentioned therein is not satisfied.</p> | <p>Actual interest payable in aggregate for one or two self-occupied properties, subject to a maximum of Rs.30,000.</p> |
|---|---|

Objective of amendment: Section 24 has been amended to provide that the monetary limit of deduction on account of interest payable on borrowed capital shall continue to apply to the aggregate of the amounts of deduction in case of more than one self-occupied houses.

- Notes:**
- (1) Scope of 'interest':** Interest includes service fee or other charges in respect of money borrowed, Hence, brokerage or commission to arrange the loan is deductible as interest on capital borrowed.
- (2) No standard deduction in case of self-occupied property:** In case of self-occupied property, statutory deduction of 30% under section 24(a) is not allowed as the NAV is NIL.
- (3)** In case certain portion of a house property is let out and the remaining portion is self-occupied, then deduction in respect of let out portion is without any limit whereas interest relating to the self-occupied portion shall be subject to Rs.30,000 or Rs.2,00,000 as the case may be.

Question 5: Self occupied properties: Mr. Naman owns two house properties one at Mumbai, wherein his family resides and the other at Delhi, which is unoccupied. He lives in Chandigarh for his employment purposes in a rented house. For acquisition of house property at Mumbai, he has taken a loan of Rs.25 lakh @ 12% p.a on 01-04-2021. He has not repaid any amount so far. In respect of house property at Delhi, he has taken a loan of Rs.6 lakh @ 11% p.a. on 01-10-2021 towards repairs. Compute the deduction which would be available to him u/s 24(b) for A.Y. 2023-24 in respect of interest payable on such loan.

Solution: Mr. Naman can claim benefit of Nil Annual Value in respect of his house property at Mumbai and Delhi, since no benefit is derived by him from such properties, and he cannot occupy such properties due to reason of his employment at Chandigarh, where he lives in a rented house.

Computation of deduction u/s 24(b) for A.Y. 2023-24 (amount in Rs):

| | |
|---|-----------------|
| (I) Interest on loan taken for acquisition of residential house property at Mumbai [25,00,000 x .12% = 3,00,000 (restricted to 2,00,000) | 200000 |
| (II) Interest on loan taken for repair of residential house property at Delhi [6,00,000 x 11 % 66,000 (restricted to 30,000) | 30,000 |
| Total Interest | 2,30,000 |
| Deduction u/s 24(b) in respect of (I) and (II) above to be restricted to - | 2,00,000 |

Question 6: Self occupied properties: BASHA has two houses, both of which are self-occupied. The particulars of these are given below:

| Particulars | (value in Rs) | |
|-------------------------------|---------------|----------|
| | House-I | House-II |
| Municipal Valuation per annum | 1,20,000 | 1,15,000 |

| | | |
|--|------------|------------|
| Fair Rent per annum | 1,50,000 | 1,75,000 |
| Standard rent per annum | 1,00,000 | 1,65,000 |
| Date of completion | 31-03-2018 | 31-03-2019 |
| Municipal taxes payable during the year (paid for House II only) | 12% | 8% |
| Interest on money borrowed for acquisition of house properties | 1,80,000 | 80,000 |

Compute Basha's income from the House Property for the Assessment Year 2023-24.

Solution: Section 23 of the Income-tax Act provides relief to the taxpayer by allowing him an option to claim nil annual value in respect of any two houses, declared as self-occupied. Besides this section 24 of the Income-tax Act provides that the monetary limit of deduction on account of interest payable on borrowed capital i.e. 30,000/ 2,00,000 shall continue to apply to the aggregate of the amounts of deduction in case of more than one self-occupied houses. Hence, the Income from house property shall be computed as under:

Computation of income from houses when they are treated as self-occupied (amount in ')

| particulars | House I and II |
|--|----------------|
| Annual Value [Since both the houses are self- occupied] | NIL |
| Less: Interest on loans [House — I: Rs.1,80,000 and House - II: Rs.80,000 (Restricted to Rs.2,00,000)] | 200000 |
| Income from house property | -200000 |

Question 7: Self-occupied properties: Mr. Y has three houses, all of which are self- occupied. The particulars of these are given below:

| particulars | (value in Rs) | | |
|--|---------------|------------|-------------|
| | House - I | House - II | House - III |
| Municipal Valuation per annum | 1,20,000 | 1,15,000 | 2,00,000 |
| Fair Rent per annum | 1,50,000 | 1,75,000 | 2,50,000 |
| Standard rent per annum | 1.00,000 | 1,65,000 | 2,40,000 |
| Date of completion | 31 -03-201 9 | 31-03-2020 | 31-03-2020 |
| Municipal taxes payable during the year (paid for House II and III only) | 12% | 8% | 10% |
| Interest on money borrowed for acquisition of house properties | 1,80,000 | 80,000 | 75,000 |

Compute Mr. X income from the House Property for the Assessment Year 2023-24.

Solution: Section 23 of the Income-tax Act provides relief to the taxpayer by allowing him an option to claim nil annual value in respect of any two houses, declared as self-occupied, instead of one such house as provided earlier. Besides this section 24 of the Income-tax Act provides that the monetary limit of deduction on account of interest payable on borrowed capital i.e. 30,000/ 2,00,000 shall continue to apply to the aggregate of the amounts of deduction in case of more than one self-occupied houses.

Thus, assessee has the following options:

Option I: House I and II self -occupied and House III - deemed to be let out.

Option II: House I and III self -occupied and House II — deemed to be let out.

Option III: House II and III self-occupied and House I -- deemed to be let out.

The lowest value of house property amongst the above options shall be offered for taxation.

Hence, the Income from house property shall be computed as under:

(1) Computation of income from houses when they are deemed to be let out (amount in Rs) -

| particulars | House-I | House-II | House-III |
|---------------------------------------|------------------|---------------|---------------|
| Gross Annual Value [Note - A] | 1,00,000 | 1,65,000 | 2,40,000 |
| Less: Municipal taxes paid [Note - B] | Nil | 9,200 | 20,000 |
| Net annual value | 1,00,000 | 1,55,800 | 2,20,000 |
| Less: Deductions under section 24 | | | |
| (a) Statutory Deduction @ 30% of NAV | 30,000 | 46,740 | 66,000 |
| (b) interest on loans — | 1,80,000 | 80,000 | 75,000 |
| Income from house | -1,10,000 | 29,060 | 79,000 |

Notes:

(A) GAV = Municipal Value or Fair Rent, whichever is higher subject to maximum of Standard Rent.

(B) Municipal taxes actually paid shall only be allowed as deduction.

(2) Computation of income from houses when they are treated as self-occupied (amount in Rs) -

| Particulars | House I & II | House I & III | House II & III |
|--|------------------|------------------|------------------|
| Annual Value [Since both the houses are self-occupied] | Nil | Nil | Nil |
| Less: Interest on loans (Restricted to 2,00,000) | 2,00,000 | 2,00,000 | 1,55,000 |
| Income from house property | -2,00,000 | -2,00,000 | -1,55,000 |

(3) Hence, the taxable value shall be arrived as under: ---

| Option | Total |
|--|-----------|
| Option I: House I and II self-occupied and House III — deemed to be let out | -1,21,000 |
| Option II: House I and III self-occupied and House II — deemed to be let out | -1,70,940 |
| Option III : House II and III self-occupied and House I — deemed to be let out | -2,65,000 |

Circumstances as per Section 25 in which interest payable outside India is not deductible.

Amounts not deductible [Section 25]: Notwithstanding anything contained in Section 24, any interest chargeable under this Act-

- which is payable outside India;
- on which tax has not been paid or deducted; and
- in respect of which there is on person in India who may be treated as an agent under section 163; shall not be allowed as deduction in computing the income chargeable under the head "Income from house property".

Question 8: Interest on borrowed capital: Arvind commenced construction of a residential house, intended exclusively for his residence, on 01-11-2021. He raised a loan of Rs.10,00,000 at 12% interest for the purpose of construction on 01-11-2021. Finding that there was an over-run in the cost of construction, he raised a further loan of Rs.12,00,000 at the same rate of interest on 1-10-2022. What is the interest allowable under section 24, assuming that the construction was completed by 31-3-2023? **(May 2000)**

Solution: According to Section 23(2), the annual value shall be taken as NIL since the house is self-occupied by the assessee.

Thus, the interest allowable (including interest relating to pre-construction period) will be subject to maximum limit of Rs.2,00,000. Pre-construction period shall start from 01-11-2021 and end on 31-03-2022 i.e. (31st March preceding the date of completion of construction).

Computation of interest allowable under section 24(b) (amounts in Rs.)

| | | |
|---|--------|-----------------|
| Total pre-construction interest | [WN-1] | 50,000 |
| Pre-construction interest allowable in assessment year 2023-24 (1/5 th of above) | | 10,000 |
| Current year interest | [WN-2] | 1,92,000 |
| Total interest | | 2,02,000 |

Hence, total amount deductible under section 24(b) = Rs.2,00,000.

Working Notes:

(1) Pre-construction interest = Rs.10,00,000 x 12% x 5 ÷ 12 (from 1-11-2021 to 31-3-2022) = Rs.50,000.

(2) Current Year (FY 2022-23) = Loan - I: Rs.10 lakhs x 12% x 1 + Loan - II: Rs.12 Lakhs x 12% x 6 / 12 = Rs.192000

COMPREHENSIVE PROBLEMS

Question 9:

Compute net annual value with the following details for the A.Y. 2023-24 :

| Particulars | H1 | H2 | H3 | H4 | H5 | H6 |
|------------------------|-------------|-------------|-------------|-------------|-------------|-------------|
| Situated at | Patna | Anand | Hyderabad | Balurghat | Jodhpur | Etawa |
| Municipal Value | Rs.1,00,000 | Rs.2,00,000 | Rs.3,00,000 | Rs.4,00,000 | Rs.4,25,000 | Rs.6,00,000 |
| Gross Annual Value | Rs.1,00,000 | Rs.2,50,000 | Rs.1,80,000 | Rs.5,00,000 | Rs.8,00,000 | Rs.5,00,000 |
| Municipal tax for P.Y. | Rs. 5,000 | 10% | 5% | 20% | 12% | 10% |
| Sewerage tax | - | 5% | Rs. 1,000 | 3% | Rs. 3,750 | Rs. 1,000 |
| Water Tax | - | 3% | 5% | 2% | 5% | - |

Additional information :

- In case of H3, municipal tax paid for the financial year 1994-95 to 2021-22 is Rs. 2,00,000.
- In case of H4, municipal tax paid for the financial year 2023-24 is Rs. 3,000.
- In case of H6, all taxes charged by municipality are paid to the extent of 80% (50% by owner and 30% by tenant).

Solution:

Computation of Net Annual Value for A.Y. 2023-24 : (Amount in Rs.)

| Particulars | H1 | H2 | H3 | H4 | H5 | H6 |
|--------------------------|----------|----------|-----------------------|---------------------|----------|---------------------|
| Gross Annual Value (a) | 1,00,000 | 2,50,000 | 1,80,000 | 5,00,000 | 8,00,000 | 5,00,000 |
| Less : (i) Municipal Tax | 5,000 | 20,000 | 2,15,000 ³ | 80,000 ¹ | 51,000 | 30,000 ² |
| (ii) Sewerage tax | - | 10,000 | 1,000 | 12,000 | 3,750 | 500 ² |
| (iii) Water Tax | - | 6,000 | 15,000 | 8,000 | 21,250 | - |

| | | | | | | |
|-------------------------------------|---------------|-----------------|--------------------|-----------------|-----------------|-----------------|
| Total (b) | 5,000 | 36,000 | 2,31,000 | 1,00,000 | 76,000 | 30,500 |
| Net Annual Value [(a) – (b)] | 95,000 | 2,14,000 | (-), 51,000 | 4,00,000 | 7,24,000 | 4,69,500 |

Municipal tax is calculated on municipal value.

Notes :

1. Though municipal tax is allowed on cash basis (only if paid by owner) but advance municipal tax is not allowed.
2. Municipal tax paid by tenant is not allowed as deduction.
3. Rs. 2,00,000 (being municipal tax of past years paid during the year) + 5% of Rs. 3,00,000 (municipal tax of current year paid during the year).

Question 10:

Calculate interest on loan allowed for assessment year 2018-19 to 2023-24 from the following information :

Loan was taken on 1/1/2014 Rs. 5,00,000 @ 12% p.a.

Construction commenced on 1/8/2014. Construction completed on 31/3/2019. Repayment made as under :

| | | | |
|--------------|--------------|--------------|--------------|
| On 1/4/2015 | On 1/4/2018 | On 1/4/2021 | On 1/7/2022 |
| Rs. 1,00,000 | Rs. 1,00,000 | Rs. 1,00,000 | Rs. 1,00,000 |

Solution :

Since construction started on 1/8/2014, hence pre-construction period starts from 1/8/2014 and since construction completed on 31/3/2019, hence pre construction period ends on 31/3/2018 and post construction period starts from the year 2018-19. Finally, pre construction period is from previous year 2014-15 to previous year 2017-18 and post construction period is from previous year 2018-19 onwards.

Thus, pre-construction period interest are as under

| Previous Year | Amount | Month | Interest @ 12% |
|---|----------|-------|-----------------|
| 2014-15 | 5,00,000 | 8 | 40,000 |
| 2015-16 | 4,00,000 | 12 | 48,000 |
| 2016-17 | 4,00,000 | 12 | 48,000 |
| 2017-18 | 4,00,000 | 12 | 48,000 |
| Total interest for pre-construction period | | | 1,84,000 |

Total interest for pre-construction period is Rs. 1,84,000 which shall be allowed in 5 equal installments i.e., Rs. 36,800 p.a. from P.Y. 2018-19 to 2022-23.

Computation of interest :

| Assessment Year | Previous Year | Pre construction period Interest | Post construction period Interest | Total Interest |
|-----------------|---------------|----------------------------------|-----------------------------------|----------------|
| 2018-19 | 2017-18 | -- | -- | -- |
| 2019-20 | 2018-19 | 36,800 | 36,0001 | 72,800 |
| 2020-21 | 2019-20 | 36,800 | 36,0001 | 72,800 |
| 2021-22 | 2020-21 | 36,800 | 36,0001 | 72,800 |

| | |
|--|-----------------|
| (C) = Higher of (A) and (B) | 2,50,000 |
| Standard Rent (D) | 1,50,000 |
| Gross Annual Value [Lower of (C) and (D)] | 1,50,000 |

Question 12:

Compute income under the head 'Income from house property' of Sri from the following information:

| Particulars | H1 | H2 | H3 | H4 |
|-----------------------|---------------|---------------|---------------|--------------|
| Used for | Self occupied | Self occupied | Self occupied | Own Business |
| Situated at | Mumbai | Abu | Kolkata | Hyderabad |
| Gross Municipal Value | 3,00,000 | 2,00,000 | 7,00,000 | 3,00,000 |
| Fair Rent | 2,00,000 | 2,00,000 | 6,00,000 | 1,20,000 |
| Standard Rent | 3,00,000 | 2,40,000 | 7,00,000 | 2,00,000 |
| Municipal Tax | 15% | 15% | 15% | 15% |
| Repairs | 13,000 | 4,000 | 8,000 | 8,000 |
| Ground Rent | 20,000 | Nil | Nil | 6,000 |
| Land Revenue | Nil | 10,000 | Nil | Nil |
| Interest on Loan | 40,000 | 10,000 | 2,10,000 | 20,000 |
| Loan taken on | 1998-99 | 1998-99 | 2019-20 | 1999-00 |

Solution :

In the given case, there are two options :

Option 1: Take H1 & H3 as Self-Occupied (S/O) and H2 as Deemed to be Let-Out (DLO)

Option 2: Take H1 as Deemed to be Let-Out (DLO) and H2 & H3 as Self-Occupied (S/O)

Option 3: Take H3 as Deemed to be Let-Out (DLO) and H1 & H2 as Self-Occupied (S/O)

Total income under the head house property shall be computed applying each option separately and then the option, which yields least income under this head, shall be opted.

| Particulars | Option1 | | Option2 | | Option3 | |
|--|-----------------------|---------------------|----------|-----------------------|----------|---------------------|
| | H1 & H3 S/O | H2 DLO | H1 DLO | H2 & H3 S/O | H3 DLO | H1 & H2 S/O |
| Gross Annual Value | Nil | 2,00,000 | 3,00,000 | Nil | 7,00,000 | Nil |
| Less : Municipal Tax (15% of Municipal value) | Nil | 30,000 | 45,000 | Nil | 1,05,000 | Nil |
| Net Annual Value (A) | Nil | 1,70,000 | 2,55,000 | Nil | 5,95,000 | Nil |
| Less : Deduction u/s 24(a) Standard deduction (30% of NAV) | Nil | 51,000 | 76,500 | Nil | 1,78,500 | Nil |
| 24(b) Interest on loan | 2,00,000 ² | 1,00,000 | 40,000 | 2,00,000 ² | 2,10,000 | 30,000 ¹ |
| Total deduction (B) | 2,00,000 | 1,51,000 | 1,16,500 | 2,00,000 | 3,88,500 | 30,000 |
| Income from house property [(A) – (B)] | (-) 2,00,000 | 19,000 | 1,38,500 | (-) 2,00,000 | 2,06,500 | (-) 30,000 |
| Income from house property | | (-) 1,81,000 | | (-) 61,500 | | 1,76,500 |

Notes:

1. In case of H1 & H2 loan was taken prior to 1/4/1999.
2. Since loan was taken for construction on or after 1/4/1999.
3. Since H4 is used for own business purpose so it is not taxable under this head.

Total income under the head Income from house property as per option 1 is (-) Rs. 1,81,000

Computation of Income from house property of Sri for the A.Y.2023-24 :

| Particulars | Details | Details | Amount |
|---|----------|----------|-------------------|
| H1 & H3 : Self-occupied u/s 23(2)(a) | | | |
| Net Annual Value | | Nil | |
| Less : Deduction u/s | | | |
| 24(b) Interest on loan | | | |
| - For H1 (Max Limit) | 30,000 | | |
| - For H2 (Max Limit) | 2,00,000 | | |
| Subject to maximum of Rs. 2,00,000 | 2,30,000 | 2,00,000 | (2,00,000) |
| H2 : Deemed to be let out u/s 23(4) | | | |
| Gross Annual Value | | 2,00,000 | |
| Less : Municipal Tax | | 30,000 | |
| Net Annual Value | | 1,70,000 | |
| Less : Deduction u/s | | | |
| 24(a) Standard Deduction (30% of NAV) | 51,000 | | |
| 24(b) Interest on loan | 1,00,000 | 1,51,000 | 19,000 |
| Income from house property | | | (1,81,000) |

Question 13:

Mr. Ajnabi has a house property in Cochin. The house property has two equal dimension residential units. Unit 1 is self occupied throughout the year and unit 2 is let out for 9 months for Rs. 10,000 p.m. and for remaining 3 months it was self-occupied. Compute his taxable income from the following details:

Municipal value Rs. 2,00,000, Fair Rent Rs. 1,60,000, Standard rent Rs. 3,00,000, Municipal tax 10% (60% paid by assessee), Interest on loan Rs. 40,000, Expenditure on repairs Rs. 20,000.

Solution:**Working**

1. Computation of Gross Annual Value (GAV)

| Particulars | Working | Unit 1 | Unit 2 |
|---|----------------------|----------|----------|
| Municipal Value | 1:1 | 1,00,000 | 1,00,000 |
| Fair Rent | 1:1 | 80,000 | 80,000 |
| Standard Rent 1:1 | 1,50,000 | 1,50,000 | |
| Reasonable Expected Rent Higher of MV & FR (RER cannot exceed SR) | Nil | 1,00,000 | |
| Actual Rent Receivable | Rs. 10,000 * 9 | - | 90,000 |
| Gross Annual Value | Higher of Step 1 & 2 | Nil | 1,00,000 |

2. Municipal tax = 10% of Rs. 2,00,000 = Rs. 20,000 being divided in the ratio 1:1 between Unit 1 and Unit 2. Out of such Municipal tax only 60% is paid, therefore, Municipal tax allowed as deduction in case of Unit 2 is only Rs. 6,000 [i.e. Rs. 20,000 * ½ * 60%].

3. Interest on loan is divided in unit A and unit B in 1:1 as both units are of equal dimension.

Computation of income from house property of Mr. Ajnabi for the A.Y. 2023-24

| Particulars | Working | Unit 1 | | Unit 2 | |
|---------------------------------------|----------|---------------|--------|---------------|--------|
| | | Details | Amount | Details | Amount |
| Gross Annual Value | 1 | Nil | | 1,00,000 | |
| Less : Municipal Tax | 2 | | Nil | | 6,000 |
| Net Annual Value | | | Nil | | 94,000 |
| Less : Deduction u/s | | | | | |
| 24(a) Standard Deduction | | Nil | | 28200 | |
| 24(b) Interest on loan | 3 20,000 | 20,000 | 20000 | 48,200 | |
| Income from house property (-) | | 20,000 | | 45,800 | |

Conclusion: Income under the head Income from house property is Rs. 25,800 (being Rs.45,800 – Rs.20,000).

Question 14:

Mr. Abul Hasan owns three houses at Ranchi. He furnishes the following particulars for the previous year 2022-23 :

House No. I : The house was constructed in 2021 and let out to a friend at a monthly rent of Rs. 10,000 upto 31.1.2023 and thereafter, it was let out at its fair rent of Rs. 15,000 per month. He has paid Rs. 15,000 as municipal taxes @ 10% of Municipal Value. He has also paid fire insurance premium of Rs. 2,000.

House No. II : Ground floor is let out @ Rs. 20,000 p.m. first floor, identical to ground floor, is occupied by him for his residence. Municipal taxes paid @ 20% amounted to Rs. 80,000.

House No. III : The house was constructed in 2011 and is used for his business. The annual value of this house is Rs. 1,00,000 and he spent Rs. 5,000 as municipal taxes and Rs. 2,000 for repairs.

Other information:

A loan of Rs. 40,00,000 has been taken on 01-6-2020 for construction of House No. II. Construction of the house was completed on 01-6-2021. He repaid the entire loan on 31-12-2022. Interest on loan is payable @ 12% p.a. Compute his income from house property for the A.Y. 2023-24.

Solution:

Computation of Income from House Property of Mr. Abul Hasan for the A.Y. 2023-24 :

| Particulars | Details | Details | Amount |
|----------------------|---------|----------|--------|
| House 1 : Let out | | | |
| Gross Annual Value | | 1,80,000 | |
| Less : Municipal Tax | | 15,000 | |
| Net Annual Value | | 1,65,000 | |
| Less : Deduction u/s | | | |

| | | | |
|---------------------------------------|----------|----------|-------------------|
| 24(a) Standard Deduction | 49,500 | | |
| 24(b) Interest on loan | Nil | 49,500 | 1,15,500 |
| House 2 : Ground Floor (Let out) | | | |
| Gross Annual Value | | 2,40,000 | |
| Less : Municipal Tax [50%] | | 40,000 | |
| Net Annual Value | | 2,00,000 | |
| Less : Deduction u/s | | | |
| 24(a) Standard Deduction | 60,000 | | |
| 24(b) Interest on loan | 2,20,000 | 2,80,000 | (80,000) |
| House 2 : First Floor (Self occupied) | | | |
| Net Annual Value | | Nil | |
| Less : Deduction u/s | | | |
| 24(b) Interest on loan | | 2,00,000 | (2,00,000) |
| House 3 : Used in own business | | | Nil |
| Income from House Property | | | (1,64,500) |

Workings :

1. Fair Rent : Since 1st house is let out by assessee to his friend @ Rs. 10,000 p.m. and the same property is let out to other tenant @ Rs. 15,000 p.m., this signifies that 2nd house has fair rent Rs. 15,000 * 12 = Rs. 1,80,000.

2. Calculation of Interest to be deducted in A.Y.2023-24

| Previous Year | Month | Interest |
|---|-------|----------|
| Pre-construction Interest | | |
| 2020-21 | 10 | 4,00,000 |
| 1/5th of pre-construction (a) | | 80,000 |
| Post-construction interest (b) [Rs. 40,00,000 × 12% × 9/12] | 9 | 3,60,000 |
| Total interest charged (a) + (b) | | 4,40,000 |
| 50% for Ground Floor | | 2,20,000 |

Deemed Ownership [Section 27]:

For the purposes of Sections 22 to 26, the following persons shall be deemed to be the owner of house property —

(1) Transfer to spouse or minor child otherwise than for adequate consideration:

(2) Holder of an impartible Estate: The holder of impartible estate shall be deemed to be the individual owner of all the properties comprised in the estate.

(3) Property allotted under house building scheme: A member of a co-operative society, company or other association of persons to whom a building or part thereof is allotted or leased under a house-building scheme of the society, company or association, as the case may be, shall be deemed to be owner of that building or part thereof.

(4) Possession on part performance of contract: A person who is allowed to take or retain possession of any building or part thereof in part performance of a contract of the nature referred to in section

53A of the Transfer of Property Act, 1882, shall be deemed to be the owner of that building or part thereof.

(5) Holder of substantial lease or other rights for not less than 12 years : A person who acquires any rights (excluding any rights by way of a lease from month to month or for a period not exceeding one year) in or with respect to any building or part thereof, by virtue of any transaction as is referred to under section 269UA(f), shall be deemed to be the owner of that building or part thereof.

Only deemed owner liable to tax: Since the above mentioned persons are the deemed owners of the property, hence the income therefrom will be assessable in their hands and not in the hands of the legal owner.

Question 15: Deemed owner: Answer the following -

- (1)** Mr. Rajesh transfers a property of market value Rs.38,00,000 to his wife out of natural love and affection. The income from such property is 2,00,000. How will the property income be taxed?
- (2)** Mr. Amit gifts a property valuing Rs.10,00,000 to his minor child. The annual income from such property is Rs.2,00,000. How will the property income be taxed? -
- (3)** What will your answer be, if in the above case Mr. Amit has gifted the house property to his minor married daughter? c
- (4)** Mr. Anuj gives his house property to Mr. Dinesh on lease for 20 years. However, the lease is to be renewed by Mr. Dinesh every year. How will the property income be taxed?
- (5)** What will your answer be if in the above case Mr. Anuj gives his house property on lease to Mr. Dinesh for 2 years and Mr. Dinesh can get the lease renewed for another year on payment of a specified sum and so on for indefinite period?

Solution: The above mentioned cases have been discussed as follows —

- (1)** In this case, Mr. Rajesh has transferred his house property to his wife in natural love and affection i.e. otherwise than for adequate consideration. Therefore, he will be the deemed owner of such property and hence income of Rs.2,00,000 will be assessed in the hands of Mr. Rajesh as 'Income from House Property'.
- (2)** Here, Mr. Amit has gifted the property to his minor child i.e. without any adequate consideration. Thus, Mr. Amit shall be the deemed owner of such property and the income of 2,00,000 from the said property shall be taxable in his hands.
- (3)** In case, an individual transfers the property without adequate consideration to his minor married daughter, then he shall not be treated as deemed owner in respect of such property as per Section 27. Hence, the income from such property will be taxed in the hands of the minor married daughter.
- (4)** In this case, the lease is for 20 years i.e. for more than 12 years, but the same is to be renewed every year by Mr. Dinesh i.e. for a period of not more than one year. Thus, Mr. Dinesh is not treated as the deemed owner of such property and the income from such property will be taxable for Mr. Anuj.
- (5)** Here, the lease is for 2 years but Mr. Dinesh can renew it after every 2 years for indefinite period, which implies that the lease can be for more than 12 years. Thus, Mr. Dinesh will be the deemed owner of such property and income therefrom will be taxable in his hands.

THE END

5. PROFITS AND GAINS OF BUSINESS OR PROFESSION

Concept of Business' and 'Professional.

1. **Business [Section 2(13)]:** 'Business' includes any trade, commerce or manufacture or any adventure or concern in the nature of trade, commerce or manufacture.

- Trade means purchase and sale of goods carried on in order to earn profits;
- Commerce means large scale trade;
- Manufacture, with its grammatical variations, means a change in a non—living physical object or article or thing,
 - (i) resulting in transformation of the object or article or thing into a new and distinct object or article or thing having a different name, character and use; or
 - (ii) Bringing into existence of a new and distinct object or article or thing with a different chemical composition or integral structure.
- **Any adventure or concern in the nature of trade, commerce or manufacture** means the transaction which cannot be properly considered as trade or business. A single isolated transaction outside the assessee's line of business may constitute an adventure in nature of trade and commerce.

Essentials of business:

- (a) Carrying of transactions or activities on regular basis.
- (b) Profit motive.
- (c) Application of labour and skill.

2. **Profession [Section 2(36)]:** 'Profession' includes vocation.

Thus, Profession means an occupation which requires intellectual or manual skill, based on regular learning & experience, exercised for earning livelihood. E.g. Legal consultancy is a profession.

"Vocation" means a work (whether systematic and organized or not) which is done on the basis of one's natural ability. It does not aim to earn any livelihood. E.g. Dancing, Singing etc. is vocation.

Incomes taxable under the head "Profits and Gains of Business or Profession" as per Section 28.

As per Section 28, the following income shall be chargeable to income-tax under the head "Profits and gains of business or profession" -

- i) Profits and Gains of any business or profession Profits and gains of any business or profession which was carried on by the assessee at any time during the previous year;
- ii) **Compensations:** Any compensation or other payment due to or received by
 - (a) any person managing the whole or substantially the whole of the affairs of an Indian company, at or in connection with the termination of his management or the modification of the terms and conditions relating thereto;
 - (b) any person managing the whole or substantially the whole of the affairs in India of any other company, at or in connection with the termination of his office or the modification of the terms and conditions relating thereto;
 - (c) any person holding an agency in India for any part of the activities relating to the business of any other person, at or in connection with the termination of the agency or the modification of the terms and conditions relating thereto;

- (d) any person, for or in connection with the vesting in the government, or in any corporation owned or controlled by the Government, under any law for the time being in force, of the management of any property or business;
- (e) any person, by whatever name called, at or in connection with the termination or the modification of the terms and conditions, of any contract relating to his business,
- iii) Income derived by a trade, professional or similar association from specific services performed for its members. (This clause is an exception to Principle of Mutuality);
- iv) **Incentives received or receivable by assessee carrying on export business:**
 - (a) **Profit on sale of import entitlements:** Profits on sale of a license granted under the Imports (Control) Order, 1955, made under the Imports and Exports (Control) Act, 1947;
 - (b) **Cash assistance against exports under any scheme of Govt:** Cash assistance received or receivable by any person against exports under any scheme of the Government of India;
 - (c) **Duty Drawback:** Any duty of customs or excise repaid or repayable as drawback to any person against exports under the Customs and Central Excise Duties Drawback Rules, 1971;
 - (d) **Profit on the transfer of DEPB:** Any profit on the transfer of the Duty Entitlement Pass Book Scheme (DEPB), being the Duty Remission Scheme under the EXIM policy;
 - (e) **Profit on the transfer of DFRC:** Any profit on the transfer of Duty Free Replenishment Certificate (DFRC), being the Duty Remission Scheme under the EXIM policy;
- v) **Benefit or perquisite arising from business or profession:** The value of any benefit or perquisite, whether convertible into money or not, arising from business or the exercise of a profession;
- vi) **Partners remuneration:** Any interest, salary, bonus, commission or remuneration, by whatever name called, due to or received by, a partner of a firm from such firm. However, where such income is not deductible in the hands of the firm u/s 40(b), the same shall not be taxable in the hands of partners to the extent deduction is not allowed;
- (va) **Non competing fees and exclusivity receipts:** Any sum, whether received or receivable, in cash or in kind, under an agreement for —
 - (a) Not carrying out any activity in relation to any business or profession i.e. for non-competing; or
 - (b) Not sharing any know-how, patent, copyright, trademark, license, franchise or any other business or commercial right of similar nature or information or technique likely to assist in the manufacture or processing of goods or provision of services i.e. exclusivity;

Exceptions: The clause (a) shall not apply in respect of sum received,

 - (i) on account of transfer of the right to manufacture, produce or process any article or thing or right to carry on any business or profession, which is chargeable as 'Capital Gains' under section 45; or
 - (ii) as compensation from the multilateral fund of the Montreal Protocol on Substances that deplete the Ozone Layer under the United Nations Environment Programme.
- vii) **Key man insurance policy receipts:** Any sum received under a Keyman Insurance Policy including the sum allocated by way of bonus on such policy;
- viii) **FMV of inventory on its conversion as capital asset:** The fair market value of inventory as on the date on which it is converted into, or treated as, a capital asset determined in the prescribed manner.

ix) Sale proceeds of assets of specified business : 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.

Speculation business distinct from general business [Explanation 2]: Where speculative transactions carried on by an assessee are of such a nature as to constitute a business, the business shall be deemed to be distinct and separate from any other business.

Mode of computation of income under the head ‘Profits and Gains of Business or Profession’ [Section 29]:

| | |
|--|------------|
| Net Profit as per Profit and Loss Account | xxx |
| Add: Expenses debited to Profit and Loss A/c but not allowable under this head. [Section 37(2B), 38, 40, 40A, 43B; expenses allowable under any other head or capital expenditure] | xxx |
| Less: Allowable Expenses under this head but not debited to Profit & Loss A/c [Section 30 to 37(1)] | xxx |
| Less: Incomes not taxable under this head but credited to Profit and Loss A/c [Section 15, 22, 45 and 56 or incomes exempt under section 10] | xxx |
| Add: incomes not credited to Profit and Loss A/c but taxable under this head [Section 28, 41] | xxx |
| Profits and Gains of Business or Profession | xxx |

Methods of accounting that can be followed for computing the business income?

Method of accounting [Section 145]: Income chargeable under the head ‘Profits and gains of business or profession’ shall be computed in accordance with either cash or mercantile system of accounting regularly employed by the assessee.

- (i) if cash system of accounting is followed, then only the incomes actually received and expenses actually paid in cash during the previous year will be considered.
- (ii) If mercantile system of accounting is followed, then the income will be computed on accrual basis, adjusting the outstanding incomes/expenses, prepaid expenses and unearned incomes.

Speculative transactions? List the transactions which are not deemed to be speculative transactions.

Speculative Transactions [Section 43(5)] : “Speculative transaction” means a transaction in which a contract for the purchase or sale of any commodity, including stocks and shares, is periodically or ultimately settled otherwise than by the actual delivery or transfer of the commodity or scrips.

The transactions which are not regarded as speculative transactions are as follows

1. Hedging contract in respect of raw materials or merchandise
2. Hedging contract in respect of stocks and shares
3. Forward contract:
4. Trading in derivatives:
5. Trading in commodity derivatives:

Deemed Speculation Business [Explanation to Section 73]:

Where any part of the business of a company consists of purchase and sale of shares of other companies, then such company shall be deemed to be carrying on a speculation business to the extent to which the business consists of the purchase and sale of such shares.

Exceptions: The said business shall not be deemed to be speculation business in the case of following companies -

- (a) A Company whose gross total income consists mainly of income under the heads "Income from house property", "Capital gains" and "Income from other sources".
- (b) A Company the principal business of which is the business of trading in shares or banking or the granting of loans and advances.

Taxability of Speculation Business [Explanation 2 to Section 28]: Where the speculative transactions carried on by an assessee are of such a nature as to constitute a business, such business shall be deemed to be distinct and separate from any other business, thus, in such case —

- Profits and gains of such business are to be shown separately;
- The loss of a speculation business can only be set off only against speculation income.
- This loss can be carried forward for 4 years.

Conditions to be fulfilled for claiming deduction of 'Losses incidental to businesses

The trading losses (other than the capital losses), incidental to business, shall be allowed as deduction while computing business income, on fulfillment of the following conditions -

- (a) Loss should be real in nature and not notional or fictitious.
- (b) The loss should be revenue loss and not capital loss.
- (c) Losses should have actually occurred during the previous year.
- (d) Loss should be incidental to business i.e. arising directly from carrying of business activities.
- (e) There should not be any direct or indirect provision in the Act prohibiting the deduction of such loss.

For example: Loss on account of embezzlement by employee or loss of goods in transit, etc. is allowed as deduction.

Deductions related building under section 30:

Rent, rates, taxes, repairs and insurance of building [Section 30]: In respect of rent rates, taxes, repairs and insurance for premises, used for the purposes of the business or profession, the following deductions shall be allowed -

- (a) **Rent and repairs of premises:** Where the premises are occupied by the assessee —
 - (i) as a tenant - rent paid for such premises; and further if he has undertaken to bear the cost of repairs to the premises, the amount paid for such repairs;
 - (ii) Otherwise than as a tenant - the amount paid by him for current repairs of the premises.
 - (b) **Taxes:** Any sums paid on account of land revenue, local rates or municipal taxes paid, subject to the provisions of Section 43B.
 - (c) **Insurance premium:** The amount of any premium paid in respect of insurance against risk of damage or destruction of the premises.
1. **Cost of repairs and current repairs of capital nature not deductible [Explanation]:** The amount paid on account of the cost of repairs referred to in (i) and (ii) above, shall not include any expenditure in the nature of capital expenditure.
 2. **Capital Expenditure on leased building - Lessee deemed owner - Entitled for depreciation:** As per Explanation 1 to Section 32, where any capital expenditure on construction, renovation, extension or improvement is incurred by an assessee, in respect of a building not owned by him but occupied

by way of lease or other right of occupancy, then the assessee shall be regarded as deemed owner in respect of such capital expenditure and shall be entitled for the depreciation on the same.

Repairs and insurance of machinery, plant or furniture [Section 31]: In respect of repairs and insurance of machinery, plant or furniture used for the purposes of the business or profession, the following deductions shall be allowed —

- (i) the amount paid on account of current repairs thereto;
- (ii) The amount of any premium paid in respect of insurance against risk of damage or destruction of such machinery, plant or furniture.

➤ **Usage of the asset:** In order to claim this deduction the assets must have been used for purposes of the assessee's own business the profits of which are being taxed. Even if an asset is used for a part of the previous year, the assessee is entitled to the deduction of the full amount of expenses on repair and insurance charges and not merely an amount proportionate to the period of use.

The word 'used' has to be read in a wide sense so as to include a passive as well as an active user. Thus, insurance and repair charges of assets which have been discarded (though owned by the assessee) or have not been used for the business during the previous year would not be allowed as a deduction.

➤ **Current repairs of capital nature not deductible [Explanation]:** The amount paid on account of the current repairs shall not include any expenditure in the nature of capital expenditure.

➤ **Repairs exclude replacement or reconstruction:** The term 'repairs' will include renewal or renovation of an asset but not its replacement or reconstruction. Also, the deduction allowable under this section is only of current repairs but not arrears of repairs for earlier years even though they may still rank for a deduction u/s 37(1).

Deduction to be computed in case the building, plant, etc. are partly used for business or profession and partly for other purpose?

Where any building, plant or furniture is not exclusively used for the purposes of business or profession, then the deductions under section 30 and 31 shall be restricted to a fair proportionate part thereof.

Hence, amount of deduction will be —

(a) In case of rent of premises = $\text{Rent paid} \times \left[\frac{\text{Annual value of part of premises used for business}}{\text{Annual value of entire premises}} \right]$.

(b) In any other case = $\text{Expenditure incurred} \times \text{Proportion of part of asset (or expenditure) used for business}$.

DEPRECIATION, WDV AND ACTUAL COST

Conditions to be satisfied for claiming depreciation under section 32

Depreciation [Section 32]: The conditions to be satisfied for claiming depreciation u/s 32 are as follows

1. Depreciation available on 'assets' and 'block of assets' As per Explanation 3 to Section 32, the expression "assets" shall mean-

(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, not being goodwill of a business or profession.

“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, not being goodwill of a business or profession.

In respect of which the same percentage of depreciation is prescribed. **[Section 2(11)]**

Plant [Section 43(3)]: Plant includes ships, vehicles, books, scientific apparatus & surgical equipment used for business and profession but does not include tea bushes or livestock or buildings or furniture and fittings.

2. **Asset must be owned wholly or partly by assessee:** Depreciation is allowed only to the owner of asset, however, registered ownership is not necessary, Depreciation is allowed in respect of fractional ownership and co-ownership also.

Exceptions:

- (a) **In case of leased building:** In case of lease, lessee is entitled to claim depreciation on any. Superstructure constructed by him on lease; or on renovation/ extension / improvement of building.
 - (b) **In case of hire purchase:** In case of hire-purchase, the depreciation on the asset is claimed by the hire-purchaser, that the depreciation is to be allowed to the user (i.e. hire purchaser) in the case of a hire purchase agreement.
3. **In case of lease transactions:** In the lease agreement the asset shall remain sole and exclusive property of the lessor and lessor can inspect and take possession of asset 'in case of default. Thus, lessor is entitled for depreciation on such leased asset .
4. **Asset must be used for the purpose of business or profession of the assessee:** Depreciation can be claimed in respect of any asset, only if it is used for the purpose of business or profession. In case only a part of the asset is used for business or profession, depreciation shall be allowed only for that part which is used for the purpose of business or profession of the assessee.
5. **Asset should be used during the relevant previous year:** In order to claim depreciation, it is mandatory that the asset must be in use during the previous year, irrespective of the degree of utilization.

Amount of depreciation:

- (a) **Use for less than 180 days:** if an asset is acquired by the assessee during the previous year and the same is put to use for less than 180 days during that previous year, then the depreciation will be limited to 50% of the depreciation allowable on such asset as per the rate prescribed in Rule 5(1).
- (b) **Use for 180 days or more:** There shall be no such restriction, depreciation will be allowed in full i.e. 100% of the amount calculated as per the prescribed rate.

Note: if the asset is used for less than 180 days in any subsequent previous year (i.e. year subsequent to the year of acquisition), then the depreciation is fully allowable.

Note: It is mandatory for an assessee to claim depreciation under section 32.

As per Explanation 5 to Section 32(1), the provisions of section 32(1) relating to claim of depreciation shall apply whether or not the assessee has claimed the deduction in respect of depreciation in computing his total Income.

Rate of depreciation on a block of intangible assets

As per Explanation 3(b) to Section 32(1), the intangible assets are: Know-how, patents, copyrights, trademarks, licences, franchises, or any other business or commercial rights of similar nature.

They are depreciated at the rate of 25%.

Goodwill of a business or profession has been specifically excluded from the definition of the block of asset hence no depreciation can be claimed on the same.

Various ‘Rates of Depreciation’ as prescribed in respect of Block of Assets

(1) Rates of depreciation [Rule 5(1)]: All assets have been divided into four main categories and rates of depreciation as prescribed by Rule 5(1) are given below:

PART A: Tangible Assets -

| | Assets | Rates |
|---|--|--------------|
| (I) | BUILDING: | |
| | Block 1. Buildings which are used mainly for residential purposes except hotels and boarding houses | 5% |
| | Block 2. Buildings which are not used mainly for residential purposes and not covered by Block (1) above and (3) below | 10% |
| | Block 3. Buildings acquired on or after 1 st September, 2002 for installing machinery and plant forming part of water supply project or water treatment system and which is put to use for the purpose of business of providing infrastructure facilities | 40% |
| | Block 4. Purely temporary erections such as wooden structures | 40% |
| (II) | FURNITURE AND FITTINGS | |
| Block 1. Furniture and fittings including electrical fittings | 10% | |
| (III) | PLANT & MACHINERY | |
| | Block 1. (a) Motor buses, motor lorries and motor taxis used in a business of running them on hire other than those covered under entry (b). | 30% |
| | (b) Motor buses, motor lorries and motor taxis used in a business of running them on hire, acquired on or after 23-03-2019 but before 01-04-2020 and is put to use before the 01-04-2020. | 45% |
| | Block 2. Aeroplanes, Aero engines | 40% |
| | Block 3. Specified air, water pollution control equipment, solid waste control equipment and solid waste recycling and resource recovery systems | 40% |
| | Block 4. Energy Saving Devices (as specified) | 40% |
| | Block 5. (i) Motor cars, other than those used in a business of running them on hire, acquired or put to use on or after 01-04-1990 except those covered under entry (ii); (ii) Motor cars, other than those used in a business of running them on hire, acquired on or after 23-08-2019 but before 01-04-2020 and is put to use before 01-04-2020. | 15% |

| | | |
|-------------------|--|-----|
| (IV) SHIPS | Block 6, Computers including computer software | 30% |
| | Block 7. Annual publications owned by assessee carrying on a profession | 40% |
| | Block 8. Books owned by assessee carrying on business in running lending libraries | 40% |
| | Block 9. Books, other than annual publications, owned by assessee carrying on a profession | 40% |
| | Block 10. Lifesaving medical equipment | 40% |
| | Block 11. Plant & machinery (General rate) | 40% |
| | Block 1. Ocean-going ships | 20% |
| | Block 2. Vessels ordinarily operating on inland waters not covered by Block (3) below | 20% |
| | Block 3. Speed boats operating on inland water | 20% |

PART B: Intangible Assets

| Assets | Rates |
|---|-------|
| Know-how, patents, copyrights, trademarks, licenses, franchises, or any other business or commercial rights of similar nature not being goodwill of a business or profession. | 25% |

Notes:

(i) Windmills and any specially designed devices which run on windmills installed on or after 14—2014 would be eligible for depreciation @ 40%. Likewise, any special devices including electric generators and pumps running on wind energy installed on or after 1-4-2014 would be eligible for depreciation @ 40%. In respect of windmills and any specially designed devices running on windmills installed on or before 31-3-2014 and any special devices including electric generators and pumps running on wind energy installed on or before 31-3-2014, the rate of depreciation is 15%.

(ii) Oil wells included in New Appendix I under Mineral Oil concerns under “III. Plant and Machinery” to be eligible for depreciation @ 15% [Notification No. 13/2016 dated 03-03-2016]
Oil wells has been included as entry (c) under sub-item (xii) “Mineral Oil concerns” under item (8) of subheading ill “Plant and Machinery” in new Appendix 1. The rate of depreciation for oil-wells included as entry (c) is 15%.

(2) Increased rate of depreciation for certain assets [Rule 5(2)]: Any new machinery or plant installed to manufacture or produce any article or thing by using any technology or other know-how developed in a laboratory owned or financed by the Government or a laboratory owned by a public sector company or a University or an institution recognized by the Secretary, Department of Scientific and industrial Research, Government of India shall be treated as a part of the block of assets qualifying for depreciation @40%.

Conditions to be fulfilled:

(i) The right to use such technology to manufacture such article has been acquired from the owner of such laboratory or any person deriving title from such owner.

(ii) The return filed by the assessee for any previous year in which [he said machinery is acquired, should be accompanied by a certificate from the Secretary, Department of Scientific and Industrial Research, Government of India to the effect that such article is manufactured by using such technology developed in such laboratory or such article has been invented in that laboratory.

(iii) The machinery or plant is not used for the purpose of business of manufacture or production of any article or thing specified in the Eleventh schedule.

The depreciation ordinarily allowable to an assessee in respect of any block of assets shall be calculated at the above specified rates on the WDV of such block of assets as are used for the purposes of the business or profession of the assessee at any time during the previous year.

Actual Cost' and the manner of its computation

Actual cost [Section 43(1)]: "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.

However, where the assessee incurs any expenditure for acquisition of any asset or part thereof in respect of which a payment or aggregate of payments made to a person in a day, otherwise than by an account payee cheque drawn on a bank or an account payee bank draft or use of electronic clearing system through a bank account or through such other electronic mode as may be prescribed, exceeds 10,000, such expenditure shall be ignored for the purposes of determination of actual cost. [(a) Credit Card; (b) Debit Card; (c) Net Banking (d) IMPS (Immediate Payment Service); (e) UPI (Unified Payment Interface); (f) RTGS (Real Time Gross Settlement); (g) NEFT (National Electronic Funds Transfer), and (h) BHIM (Bharat Interface for Money) Aadhar Pay have been prescribed as mode of electronic payment]

Manner of computation of Actual Cost:

| | |
|--|------------|
| Purchase price of the asset | xxx |
| Add: Direct costs attributable to bring asset to its present location and working condition for its intended use (i.e. expenses incurred for acquiring the asset E.g.- freight, insurance, loading and handling etc. and expenses incurred in connection with the installation of the asset.) | xxx |
| Add: Interest on capital borrowed in connection with the acquisition of asset before the asset is first put to use. [Explanation 8] | xxx |
| Less: Amount of duty of excise or additional duties of customs levied on it and included in its cost, in respect xxx of which claim of CFNVAT credit has been made and allowed under the CENVAT Credit Rules, 2004. [Explanation 9] | |
| Less: Portion of cost of asset which has been met directly or indirectly by the Central Government or a State xxx Government or any authority under any law or any other person, in the form of a subsidy or grant or reimbursement. However, if such subsidy or grant or reimbursement is not directly relatable to the acquisition of the asset, then the amount to be reduced from the cost of the asset shall be — Amount to be deducted = $\frac{\text{Total amount of subsidy/grant/reimbursement} \times \text{cost of that Asset}}{\text{Total cost of the assets for which subsidy/grant/reimbursement is given}}$ | |
| [Explanation 101] | |
| Add/Less: Increase or decrease in cost due to exchange rate fluctuation [Section 43A] | xxx |
| Actual Cost of the asset for purpose of Section 43(1) | xxx |

| Various situations when the actual cost of an asset is taken at notional figures | | |
|--|---|--|
| Exp | Circumstances | Actual Cost |
| 1. | Scientific research asset used for business: Asset is used in the business after it ceases to be used for scientific research related to that business. | Actual Cost as reduced by deduction allowed under section 35(i)(iv) (i.e. NIL). |
| (4) | Inventory converted into capital asset and used for business or profession: Where inventory is converted or treated as a capital asset and is used for the purpose of business or profession, | The fair market value of such inventory as on the date of its conversion into capital asset determined in the prescribed manner, shall be the actual cost of such capital asset to the assessee. |
| 2. | Asset acquired by way of gift or inheritance. | Actual Cost to the previous owner as reduced by the amount of depreciation allowed to him (i.e. WDV). |
| 3. | Second hand asset: Where the assets constitute the business assets earlier used by any other person (i.e. second hand assets), and the Assessing Officer is satisfied that the main purpose of the transfer of such assets was the reduction of tax liability by claiming depreciation on enhanced cost. | Actual cost as determined by Assessing Officer with the previous approval of the Joint Commissioner, having regard to all the circumstances of the case. |
| 4. | Reacquisition of asset: 'Where assessee had transferred asset (which had once been owned and used by him for his business aid profession) and now, the same is reacquired by him, | Lower of: (a) WDV at the time of the original transfer; or (b) Price paid for reacquiring it. |
| (4A) | Sale & lease back: Assessee X purchases an asset belonging to Y, who had earlier claimed depreciation on such asset, subsequently leases/hires the same to Y. | Cost to X shall be the WDV of the assets to Y at the time of transfer. Explanation 4A overrides Explanation 3: In the Explanation 4A, a non-obstante clause has been included to the effect that Explanation 4A will have an overriding effect over Explanation 3. The result of this is that there is no necessity of finding out whether the main purpose of the transaction is reduction of tax liability. Explanation 4A is activated in every situation described above without inquiring about the main purpose. |
| 5. | Building converted to be used for business: Building previously the property of the assessee, is now brought into use for the purpose of business of the assessee. | Actual cost of the building as reduced by the depreciation that would have been allowed, had the asset been used for business purpose since the date of its acquisition. |

| | | |
|-------------|---|--|
| | Note: Rate of depreciation applicable in previous year of bringing the asset into business use is applied. | |
| 6. | Capital asset acquired from holding' subsidiary company: Capital asset transferred by holding co. to its subsidiary- co. or vice-versa, satisfying the conditions prescribed under section 47(iv)/47(v). | Cost to transferee company shall be the cost to the transferor company had it continued to hold the asset for its business purpose. |
| 7. | Amalgamation Capital asset transferred by amalgamating company to the amalgamated company and the amalgamated company is an Indian company. | Cost to amalgamated company shall be the cost to the amalgamating company had it continued to hold the asset for its business purpose, |
| (7A) | Demerger Transfer of capital asset in a scheme of demerger, by a demerged company to the resulting company and resulting company is an Indian company. | Cost to resulting company shall be the cost to the demerged. company had it continued to hold the asset for its business purpose. |
| 11. | Asset brought by non-resident: An asset acquired outside India by a non-resident, and subsequently brought to India and. used for the purpose of his business and profession in India. Note: Depreciation is computed at rates that would have been allowable had the asset been used in India for his business / profession since the date of its acquisition. | Actual cost as reduced by the depreciation that would have been allowed, had the asset been used in India for the said purpose since the date of its acquisition. |
| 12. | Capital asset acquired under a scheme for corporatization of Recognised Stock Exchange in India, approved by SEBI. | Cost of asset to such. stock exchange had there been no such corporatization. |
| 13. | Capital asset on which deduction has been allowed or is allowable under section 35AD. | Nil, - (a) in the case of such assessee; or (b) if the asset is acquired or received, (i) by way of gift or will or an irrevocable trust; (ii) on any distribution on liquidation of the company; and (iii) by mode of transfer referred u/s 47(i)/(iv)/ (v)/ (vi)/ (vib)/ (xiii)/ (xiiib)/ (xiv). However, where any capital asset in respect of which deduction or part of deduction allowed u/s 35AD is deemed to be the income of the assessee in accordance with the provisions of Section 35AD(7B), the actual cost of the asset to the assessee shall be the actual cost to the |

assessee, as reduced by an amount equal to the amount of depreciation calculated at the rate in force that would have been allowable had the asset been used for the purpose of business since the date of its acquisition.

Question 1: Computation of depreciation — Impact of cash payment on actual cost: From the following, data, calculate the depreciation admissible to an individual carrying on trading business:

| | Amount in Rs. |
|--|------------------|
| Plant and Machinery (Block Rate 15%) (WDV of Plant A and Plant 13 on 01-04-2022) | 25,00,000. |
| Additions -. Plant C on 30-06-2022 (Rs.5,00,000 is paid in cash and balance Rs.10,00,000 is paid through account payee cheque) - | 15,00,000 |
| Plant D on 31-12-2022 (Rs.4,80,000 is paid in cash and balance Rs.7,20,000 through RTGS transfer) | 12,00,000, |
| Sales - Plant A on 01-12-2022 | 6,00,000 |

Solution: Where the assessee incurs any expenditure for acquisition of any asset or part thereof in respect of which a payment or aggregate of payments made to a person in a day, otherwise than by an account payee cheque drawn on a bank or an account payee bank draft or use of electronic clearing system through a bank account, exceeds Rs.10,000, such expenditure shall be ignored for the purposes of determination of actual cost.

Thus, Actual cost of Plant C will be Rs.10,00,000 i.e. [Rs.15,00,000 - Rs.5,00,000] and Plant D will be [Rs.12,00,000 - Rs.4,80,000] = Rs.7,20,000

Computation of the amount of depreciation allowable (amounts in Rs.)

| | |
|--|------------------|
| WDV as on 01-04-2021 | 25,00,000 |
| Add: Actual cost of asset acquired during the year — | |
| 30-06-2022 | 10,00,000 |
| 31-12-2022 | 7,20,000 |
| | 42,20,000 |
| Less: Sale proceeds of Plant A on 1-12-2022 | 6,00,000 |
| WDV | 36,20,000 |
| Less: Depreciation (7.5% of ₹ 7,20,000 and 15% of ₹ 29,00,000) | 4,89,000 |
| Depreciated value as on 31-03-2023 | 31,31,000 |

Working Note: Depreciation is allowed to the extent of 50% as the asset is used for less than 180 days during the previous year. Thus, depreciation on Plant D acquired on 31-12-2022 shall be allowed @ 7.5% of Rs.7, 20,000.

Question 2: Conversion of use of building — Depreciation:

Compute the amount of depreciation allowable in the following cases — Dr. Jolly purchased a house property on 1-12-2020 for Rs.10, 00,000 till 1-12-2022, the same was self-occupied as a residence. On this date the building was brought into use for his medical profession. Rate of depreciation on buildings at the time of purchase of house property was 15%.

Solution: As per Explanation 5 to section 43(1), building previously the property of the assessee, is now brought into use for the purpose of business of the assessee, the actual cost shall be the actual cost of the building as reduced by the depreciation that would have been allowed, had the asset been used for business purpose since the date of its acquisition. The rate of depreciation to be applied is the rate in force in the year in which building is brought into business use i.e. 10%.

Computation of the amount of depreciation allowable (amounts in Rs.) -

| | |
|---|------------|
| WDV as on 31-3-2021 | 9,50,000 |
| Less: Depreciation @ 5% of 10,00,000 [WNJ] | |
| WDV as on 01-04-2021 | |
| Less: Depreciation (10% of ? 9,50,000) | |
| WDV as on 1-4-2022 (Actual cost of building) | — 8,55,000 |
| Depreciation for the current year (10% of ? 8,55,000) | 85,500 |

Working Note Depreciation is allowed to the extent of 50% as the asset is used for less than 180 days during the previous year.

Question 3: Computation of depreciation: A car purchased by S on 10-08-2017 for Rs.3,25,000 for personal use is brought into the business of the assessee on 01-12-2022, when its market value is Rs.1,50,000. Compute the actual cost of the car and the amount of depreciation for the assessment year 2022-23 assuming the rate of depreciation to be 15%.

Solution: As per Explanation 5 to section 43(1), building previously the property of the assessee, is now brought into use for the purpose of business of the assessee, the actual cost shall be the actual cost of the building as reduced by the depreciation that would have been allowed, had the asset been used for business purpose since the date of its acquisition. However, it does not provide any mode for a motorcar which is brought into business use after being initially used for personal purposes.

Therefore, Actual cost of motorcar brought into business use actual cost to assessee = Rs.3,25,000. (The market value of motorcar as on date of bringing it into business use is irrelevant)

Thus, actual cost of car = Rs.3,25,000 & depreciation = 7.5% of 3,25,000 = Rs.24,375 (since the car was used for less than :180 days in the previous year).

Written down value [Section 43(6)]:

Written down value (WDV) means —

- (i) **In case of assets acquired in the previous year:** Actual cost to the assessee.
- (ii) **In case of assets acquired before the previous year:** Actual cost to the assessee less depreciation actually allowed to him (including unabsorbed depreciation, if any).

WDV be determined in case of 'Block of Assets'.

WDV of block of assets shall be computed as follows

| | |
|---|-----|
| Aggregate of Written down Value of all the assets falling within the block of assets as at the beginning of the previous year | xxx |
| Add: Actual cost of any asset falling within that block not being increase on account of acquisition of goodwill of a business or profession, acquired during the previous year | xxx |
| Less: | |

| | |
|--|-----|
| (i) Moneys payable (including scrap) in respect of any asset falling within that block which is sold, discarded, demolished or destroyed during the previous year, to the extent it does not exceed the sum of the above two. | xxx |
| (ii) Where goodwill of a business or profession was part of the block of assets on which depreciation was allowed to the assessee up to previous year 2020-21, actual cost of the goodwill as reduced by amount of depreciation that would have been allowable to the assessee for such goodwill as if goodwill was the only asset in the block. However, such amount of reduction cannot exceed the WDV | xxx |
| WDV at the end of the year | xxx |
| Less: Depreciation at block rate | xxx |
| Depreciated value of the block at the end of year | xxx |

Note: In CIT v. Kasturi and Sons Ltd. [1999] 237 ITR 24 (SC) it has been held that the expression “moneys payable” has to be interpreted only as actual moneys payable in cash or cheque/draft and. not any other thing or benefit which can be converted into money.

WDV in case of ‘Slump Sale’

“Slump sale” means transfer of one or more undertaking, by any, means, for a lump sum consideration without values being assigned to the individual assets and. liabilities in such sales. The WDV shall be calculated as follows -

| | |
|--|-----|
| WDV of Block of assets | xxx |
| Less: Deduction on account of slump sale to the extent of amount computed as under (Sec Note) | xxx |
| WDV of block of assets eligible for depreciation | xxx |

Note: Deduction on account of slump sale is computed as follows

| | |
|---|-----|
| Actual cost of assets falling in the Block, which is transferred by slump sale | xxx |
| Less: Depreciation that would have been allowed if that asset was the only one in the block | xxx |
| Deduction on account of slump sale | |
| Deduction on account of slump sale | xxx |

WDV be determined of the block f assets in case the block is transferred in succession of business or profession

In case a block is transferred in succcs3ion of business or profession, WDV shall he —

| No. | Cases | WDV |
|-----|--|---|
| (1) | WDV in hands of successor under section 170 | = WDV in hands of the predecessor. |
| (2) | WDV in hands of transferee company [being holding / subsidiary company, where transfer made fulfills the conditions under section 47(iv)/ (v)] | = WDV in hands of transferor company. |
| (3) | WDV in hands of amalgamated Indian company | = WDV in hands of amalgamating company. |

| | | | |
|-----|---|---|---|
| (4) | WDV of assets transferred to resulting company Note: The WDV of the assets so transferred to resulting company shall be reduced from the WDV of demerged company on the 1 st day of the previous year. | = | WDV in hands of demerged company. |
| (5) | WDV in hands of company formed by corporatisation of recognized stock exchange | = | WDV in the hands of such recognised stock exchange immediately before such corporatisation. |
| (6) | Actual cost of block of assets transferred to the limited liability partnership [in case transfer made fulfills the conditions under section 47(xiiib)] | = | WDV of the block of assets in the hands of the transferor private/unlisted company on the date on which the company got converted into LLP. |

Admissibility of depreciation if – (1) Block exists but WDV ceases to exist; or (2) WDV exists but the block ceases to exist.

Ans: Since, existence of the block of assets as well as positive WDV are the two basic requirements for claiming depreciation, hence, no depreciation shall be allowed in case either of them ceases to exist.

(1) Block exists but WDV ceases to exist: In case written down value of a block of assets ceases to exist i.e. becomes zero, but the block still exists, then there will be no allowance of any depreciation. Further, the amount of sale price over and above the written down value of block of assets, shall be treated as short-term capital gains.

(2) WDV exists but the block ceases to exist: In case WDV exists but the block of assets ceases to exist i.e. no asset exists in such block, then also there will be no allowance of any depreciation. Further, the balance amount of WDV, shall be treated as short-term capital loss under the law.

Question 4: WDV exists but there is no asset in the block: WDV of the block as on April 1, 2022 is Rs.15,00,000; rate of depreciation = 15%

(i) Assets, falling within the block, are purchased during the year for Rs.5,00,000.

(ii) Sale of entire block = Rs.8,80,000. Determine the tax consequences.

Solution: WDV of the block as on 31st March 2023 amounts in Rs.)

| | |
|--|------------------|
| Opening WDV | 15,00,000 |
| Add: Actual cost of the asset acquired during the year | 5,00,000 |
| | 20,00,000 |
| Less: Moneys payable in respect of entire block sold during the year | 8,80,000 |
| WDV as on 31-3-2022 (as block ceases to exist) | - |
| Depreciation admissible | - |
| Short term capital Loss (Rs.20,00,000 – Rs.8,80,000) | 11,20,000 |

Question 5: Block exists but there is no WDV: Mr. Prakash has the following which are eligible for depreciation at 15% on written down value (WDV) basis:

| | | |
|------------|--------------------------------|-------------|
| 01-04-2019 | WDV of plant 'X' and Plant 'Y' | Rs.2,00,000 |
| 10-12-2022 | Acquired a new plant 'Z' for | Rs.2,00,000 |

| | | |
|--|--------------------|-------------|
| 22-01-2023 | Sold Plant 'Y' for | Rs.4,00,000 |
| Expenditure incurred in connection with transfer | | Rs.10,000 |
| Compute eligible depreciation claim / chargeable capital gain if any (7 marks, PCC May 2010) | | |
| Solution: Computation of capital gain / depreciation claim of Mr. Prakash (Amount in Rs.) | | |
| Sale proceeds of Plant Y | | 4,00,000 |
| Less: Deduction under section 50(1) | | |
| Purchase of new Plant 'Z' | 2,00,000 | |
| WDV as on 1-4-2022 of Block comprising of Plants 'X' and 'Y' [WN-1] | 1,22,825 | |
| Expenditure incorrect in connection with such transfer | 10,000 | 3,32,825 |
| Short-term capital gains for 2022-23 (Assessment Year 2023-24) | | 67,173 |

Working Notes:

1. Computation of WDV:

(amount in Rs.)

| | |
|--|----------|
| WDV as on 1-4-2019 of Block comprising of Plants 'X' and 'Y' | 2,00,000 |
| Less: Depreciation for previous year 2019 - 20 @15% | 30,000 |
| WDV as on 1-4-2020 | 1,70,000 |
| Less: Depreciation for previous year 2020-21@ 15% | 25,500 |
| WDV as on 14-2021 | 1,44,500 |
| Less: Depreciation for P.Y 2021 - 22 @15% | 21,675 |
| WDV as on 14-2022 | 1,22,825 |

2. Since the block is reduced to Nil, hence, no depreciation shall be admissible for assessment year 2023-24.

Question 6: Computation of depreciation": From the following data calculate the depreciation admissible to and; individual carrying on trading business (amount in Rs.)

| | |
|--|----------|
| Factory Building (WDV) | 5,00,000 |
| Plant and Machinery (WDV) | 8,00,000 |
| Additions 30-06-2022 | 1,00,000 |
| 31-12-2022 | 1,00,000 |
| Sales 01.12.2022 | 6,00,000 |
| Computer Addition 1 – 1 – 2023 (Rs.60,000 is paid through A/c payee cheque and balance in 'cash) | 80,000 |
| Furniture and Fixtures (WDV) | 1,00,000 |
| Motor-car (WDV) | 60,000 |

(Nov. 2000)

Solution: The admissibility of depreciation shall be computed as follows

(amount in Rs.)

| Particulars | Block 1- Plant & Machinery & Motor Car (15%) | Block 2- Furniture & Fittings (10%) | Block 3- Factory Building (10%) | Block 5- Computer (40%) |
|--------------------|--|-------------------------------------|---------------------------------|-------------------------|
| WDV as on 1-4-2022 | 8,60,000 | 1,00,000 | 5,00,000 | Nil |

| | | | | |
|---|------------------|-----------------|-----------------|---------------|
| Add: Actual cost of asset acquired during the year -.30-06-2022 | 1,00,000 | Nil | Nil | Nil |
| 31-12-2022 & 1-1-2023 | <u>1,00,000</u> | <u>Nil</u> | <u>Nil</u> | <u>60,000</u> |
| | 10,60,000 | 1,00,000 | 5,00,000 | 60,000 |
| Less: Sales (1-12-2022) | <u>6,00,000</u> | <u>Nil</u> | <u>Nil</u> | <u>Nil</u> |
| WDV as on 31-3-2023 | 4,60,000 | 1,00,000 | 5,00,000 | 60,000 |
| Less: Depreciation at block rate | <u>61,500</u> | <u>10,000</u> | <u>50,000</u> | <u>12,000</u> |
| WDV as on 1-4-2023 | 3,98,500 | 90,000 | 4,50,000 | 48,000 |

Working Notes:

- (1) Since assessee is carrying on trading business, no additional depreciation is admissible,
- (2) Since the new plant acquired during the previous year is put to use for less than 180 days depreciation on such plant is calculated at half of the block rate, Hence, depreciation on Plant & Machinery and motor car = 15% of Rs.3.6 lakh + 50% of 15% of Rs.1 lakh (since used for less than 180 days) = Rs.61,500
- (3) Though purchase price of computer is Rs.80,000 but Rs.20,000 is paid in cash, hence its actual cost will be Rs.80,000 - Rs.20,000 = Rs.60,000. Since the new computer acquired during the previous year is put to use for less than 180 days, hence depreciation on such computer is calculated at half of the block rate. Depreciation on computer = 50% of 40% of Rs.60,000 = Rs.12,000.

Question 7: Computation of depreciation: A newly qualified Chartered Accountant. Mr. Madhan, commenced practice and has acquired the following assets in his office at the cost shown against each item. Calculate the amount of depreciation that can be claimed from his professional income

| No. | Description " | Date of Acquisition | Date when put to use | Amount (Rs.) |
|-----|---|---------------------|---------------------------------------|--------------|
| (a) | Computer | 27 Sept., 2022 | 2 Oct., 2022 | 35,000 |
| (b) | Computer software | 2 Oct., 2022 | 4 Oct., 2022 | 8,500 |
| (c) | Computer Printer | 2 Oct., 2022 | 3 Oct, 2022 | 12,500 |
| (d) | Books of which books being annual Publications are of Rs.12,000) | 1 Apr., 2022 | 1 Apr., 2022 | 13,000 |
| (e) | 'Office furniture' Acquired from practicing C.A.) | 1 Apr., 2022 | 1 Apr., 2022 | 3,00,000 |
| (f) | Laptop | 26 Sept, 2022 | 4 Oct., 2022 | 43,000 |
| (g) | Fire extinguisher | 1 Apr., 2022 | No instance arose to use F.Y. 2022-23 | 2,500 |
| (h) | Purchased practicing CA's office in April 2021 who had run it for 4years, for Rs.5 lakhs which includes Rs.2 lakhs for goodwill and 3 lakhs for cost of furniture (included in (e) above) - | | | |

Note: Depreciation is to be provided at 'the applicable rates. (Take 365 days in a year)

(8 Marks, May 2007)

Solution:

| Particulars | Block 1 (Computer, Computer software, laptop & Books being non- annual publications, Books being Annual publications & Computer Printer) - 40% | Block 2 (Furniture) — 10% | Block 4 Fire Extinguisher) — 15% |
|--|---|---------------------------------|---|
| Assets put to use for 180 days or more | 60,500 | 3,00,000 | 2,500 |
| Assets put to use for less than 180 days — | 51,500 | Nil | Nil |
| Allowable Depreciation | 34,500 | 30,000 | 375 |

Working Notes:

- (1) Goodwill of profession is not eligible for depreciation.
- (2) Depreciation on fire extinguisher will be available even if it is not actually put to use because of its nature.
- (3) Computer printer is eligible for depreciation at the rate of computer.

Question 8: Computation of depreciation: Mr. k resides in Delhi. As per new rule in the city, private cars can be plied in the city only on alternate days.

He has purchased a car on 21-09-2022, for the purpose of his business as per following details:

| | Rs. |
|------------------------------|------------------|
| Cost of car (excluding GST). | 12,00,000 |
| Add: Delhi GST at 14% | 1,68,000 |
| Add: Central CST at 14% | 1,68,000 |
| Total price of car | 15,36,000 |

He estimates the usage of the car for personal purposes will be 25%. He is advised that since the car has run only on alternate days, depreciation, which is otherwise allowable, will actually be allowed.

He has started using the car immediately after purchase.

Determine the depreciation allowable on car for the assessment year 2023 - 24, if this is the only asset in the block.

If this car were to be used in the subsequent assessment year 2024-25, on the same terms and conditions above, What will be the depreciation allowed? Assume that there is no change in the legal position under the income – tax Act, 1961

(4 Marks, Nov. 2018 – NS)

Solution: According to Section 32, if an asset is acquired by the assessee during the previous year and the same is put to use for less than 180 days during that previous year, then the depreciation will be limited to 50% of the depreciation allowable on such asset as per the rate prescribed in Rule 5(1). Since the car was ready for use for more than 180 days, the date of purchase being 21-09-2022 (the date when car was put to use), hence depreciation will be allowed on such car at full rate.

Since, no input tax credit is admissible of CGST and SCST paid in respect of motor vehicles (subject to certain exceptions), the actual cost of car shall be Rs.15,36,000.

Where any motor car is not exclusively used for the purposes of business or profession, then the deduction u/s 32 shall be restricted to a fair proportionate part thereof which is used for the purpose of business. The amount of depreciation actually allowed shall be reduced from the written down value to find out depreciated value of the block of asset.

Thus, taking into account the above observations depreciation shall be computed as under (amount in Rs.)

| | | |
|---|----------|------------------|
| Assessment Year 2023-24: | | |
| Actual cost of car | | 15,36,000 |
| Less: Depreciation @15% of Rs.15,36,000 | 2,30,400 | |
| Less: Disallowed as per Section 38(2) for personal use [25%] | 57,600 | 1,72,800 |
| Depreciated value of the block at the end of year | | 13,63,200 |
| Assessment Year 2024-25: | | |
| Depreciated value of the block at the beginning of year | | 13,63,200 |
| Less: Depreciation @ 15% of Rs.13,63,200 | 2,04,480 | |
| Less: Disallowed as per Section 38(2) for personal use [25%] | 51,120 | 1,53,360 |
| Thus, Depreciated value of the block at the end of year | | 12,09,840 |
| Thus, depreciation allowable for A.Y. 2023-24 is Rs.1,72,800 and for A.Y. 2024-25 is Rs.1,53,360, | | |

Treatment of Exchange Rate Fluctuations arising in case of purchase of an asset from outside India.

Special provisions consequential to changes in rate of exchange of currency [Section 43A]: The provisions of this section are as follows —

- (1) Applicability:** The provisions of this section apply in case the assessee fulfills the following conditions
- An asset is acquired from outside India for his business and profession.
 - Subsequently, after the date of acquisition, there is change in the rate of exchange during any previous year.
 - Such exchange rate fluctuation results in increase or reduction in the liability of the assessee (as expressed in Indian currency) at the time of making the payment
 - Towards the whole or part of the cost of the asset; or
 - Towards the repayment (along with interest) of whole or part of the moneys borrowed by him from any person in any foreign currency specifically for acquiring the asset.
- (2) Treatment:** The amount by which the liability is so increased or decreased (along with increase/decrease in interest) at the time of making payment, shall be added to or reduced from the following —
- Actual cost of the asset; or
 - Capital expenditure incurred on scientific research as referred to under Section 35(1)(iv); or
 - Capital expenditure on family planning incurred by a co. as referred to under Section 36(1)(ix); or
 - Cost of acquisition of a capital asset (other than depreciable assets referred to in Section 50), while computing capital gains under Section 48.

The amount so arrived at after such addition or deduction shall be taken to be the actual cost of the asset or the amount of capital expenditure.

(3) Other relevant points:

- These adjustments are to be made only on actual payment by the assessee towards the cost of asset or repayment of the loan/interest irrespective of the method of accounting adopted by the assessee.

- (b) Where whole or part the liability is not met by assessee but is met by any other person, no adjustments of exchange rate fluctuations shall be made with respect to the liability so met.
- (c) Where assessee has entered into forward exchange contract with “authorized dealer” for purchase of foreign currency to discharge the liability as referred above, the increase or decrease in liability is computed with reference to rate of exchange specified in the contract.
- (d) Increase/decrease in liability of interest payment on account of exchange rate fluctuations will form part of cost of asset.

APPORTIONMENT OF DEPRECIATION, ADDITIONAL DEPRECIATION & UNABSORBED DEPRECIATION

Depreciation be apportioned in case of succession of business or amalgamation / demerger of a company?

In case of succession of firm or proprietary concern by a company as referred to in Section 47(xiii)/ (xiv); or succession under section 170; or amalgamation or demerger of a company; or conversion of a private/unlisted company into a limited liability partnership under section 47(xiiib), the provisions for allowability of depreciation shall be as under —

- (1) The amount of depreciation in any previous year, on tangible and intangible assets, allowable to predecessor and successor; or to amalgamating company and amalgamated company; or to demerged company and resulting company, shall not exceed the depreciation calculated at prescribed rates, had been such succession or amalgamation or demerger not taken place.
- (2) Such depreciation determined shall be apportioned between predecessor and successor, or amalgamating company and amalgamated company, or demerged company and resulting company, in the ratio of the number of days of use of assets by them during that previous year.

Question 6: Apportionment of Depreciation Mr. Gopi carrying on business as proprietor converted the same into a limited company by name Gopi Pipes (F) Ltd. from 01-07-2022 The details of the assets are given below:

| | Rs. |
|--|------------|
| Block - I WDV of plant & machinery (rate of depreciation @15%) | 12,00,000' |
| Block - II WDV of building (rate of depreciation @10%) | 25,00,000 |

The Company Gopi Pipes (P) Ltd. acquired plant and machinery in December 2022 for Rs.10,00,000. It has been doing the business from 01.07.2022.

Compute the quantum of depreciation to be claimed by Mr. Gopi and successor Gopi Pipes (P) Ltd. for the A.Y. 2022-23.

Note: Ignore additional depreciation. **(4 Marks, Nov. 2014)**

Solution: The amount of depreciation in any previous year, on tangible and intangible assets, allowable to Sole Proprietor and Private limited company shall be maximum upto the depreciation calculated at prescribed rates, had such conversion not taken place. Such depreciation shall be apportioned between predecessor and successor, in the ratio of the number of days of use of assets by them during that previous year.

Apportionment of Depreciation: No. of days in the year = 365; Date of conversion = 01-07-2021

| Asset | Total Depreciation (WDV on 1-4-2022 x Dep. Rate) | Total Days used | Days used by Gopi Proprietor | Days used by Gopi Pipes (P) Ltd. | Allowable Depreciation to Gopi Proprietor | Allowable depreciation Gopi Pipes (P) Ltd. |
|-------------------------|--|-----------------|------------------------------|----------------------------------|---|--|
| Buildings | 2,50,000 | 365 | 91 | 274 | 62,329 | 1,87,671 |
| Plant & Machinery | 1,80,000 | 365 | 91 | 274 | 44,877 | 1,35,123 |
| New Plant and machinery | 75,000 | - | - | Less than 180 days | - | 75,000 |
| | 5,05,000 | | | | 1,07,206 | 3,97,794 |

Additional depreciation [Section 32(1)(ia)]:

The provisions relating to additional depreciation are as under

(1) Applicability : Additional depreciation is available on new machinery or plant (other than ships and aircraft), which has been acquired and installed after 31-3-2005,

(a) This provision is applicable only in case of an assessee engaged in the business of manufacture or production of any article or thing or in the business of generation, transmission or distribution of power.

(b) It is applicable to only those assessee who claim depreciation on block of assets under section 32(1)(ii).

(2) Deduction: A further deduction of 20% of actual cost of such plant and machinery is allowed. However, in case the asset acquired during previous year is put to use for a period of less than 180 days then additional depreciation on such asset will be calculated @ 10% of actual cost.

Allowance of balance 50% additional depreciation : Where an asset is acquired by the assessee during the previous year and is put to use for the purposes of business for a period of less than 180 days in that previous year, and the additional depreciation in respect of such asset is restricted to 10% of the actual cost for that previous year, then, the deduction for the balance additional depreciation i.e. 10% of the actual cost of such asset shall be allowed in the immediately succeeding previous year in respect of such asset.

(3) No Deduction: Additional depreciation is not allowed in respect of the following -'

(a) Plant and machinery which, before its installation by assessee, was used whether in India or outside India by any other person;

(b) Any office appliances or road transport vehicles.

(c) Plant or machinery installed in the office premises or the residential accommodation (including the guest houses).

(d) Plant and machinery whose whole of [he actual cost is deductible (by way of depreciation or otherwise) in computing income under this head of any one previous year.

Question 7: Computation of Depreciation and additional depreciation: RP Ltd. was incorporated on 31.12.2021 for manufacture of tyres and tubes for motor vehicles in Rajasthan. The manufacturing unit was set up on 30-4-2022. The company commenced its operations on 01-05-2022. The total cost of the plant and machinery installed in the unit is Rs.10 crores. The said plant and machinery included second hand plant and machinery bought for Rs. 1 crores and, new Plant and machinery for scientific research relating to the business of the assessee acquired at a cost of Rs.1 crores. Out of the said plant and machinery, new plant and machinery acquired at cost of Rs.2 crores was put to use on 14-3-2022. Compute the amount of depreciation allowable u/s 32 of the income tax Act, 1961 in respect of the assessment year 2023-24 and assessment year 2024-25. Furnish explanations in support of your computation. **(4 Marks, May 2007)**

Solution: Computation of depreciation allowable for the assessment year 2023-24 to GP Ltd.

(Rs. crores):

| | | |
|--|----------|-------------|
| Total cost of plant and machinery | 10 | |
| Less: Used for Scientific Research [WN-1] | <u>1</u> | |
| Cost eligible for normal depreciation | <u>9</u> | |
| Normal depreciation at 15% of Rs.7 crores (since put to use for not less than 180 days) | 1.05 | |
| Normal depreciation at 7.5% of Rs.2 crores (since put to use for less than 180 days) | 0.15 | 1.20 |
| Additional Depreciation: | | |
| Cost of plant and machinery | 10 | |
| Less: Second hand plant and machinery [WN-2] | 1 | |
| Plant and machinery used for scientific research [WN-2] | <u>1</u> | |
| Cost eligible for additional depreciation | <u>8</u> | |
| Additional Depreciation at 20% of actual cost of Rs.6 crores (put to use not less than 180 days) | 1.2 | |
| Additional Depreciation at 10% of actual cost of Rs.2 crores (put to use for less than 180 days) | 0.2 | 1.40 |
| Depreciation allowable for AY 2023-24 under section 32 | | 2.60 |
| Depreciated value of plant and machinery [Rs.9 crores – Rs.2.6 crores] | | 6.40 |

Computation of depreciation allowable for the assessment year 2024 – 25 to GP Ltd. (Rs. crores)

| | | |
|--|-------------|-------------|
| Depreciated value of Plant and machinery as on 01-04-2023 | | 6.40 |
| Normal depreciation at 15% of Rs.6.4 crores | 0.96 | |
| Additional Depreciation: Cost of plant and machinery [Rs.2 crores x 10%] [WN-3] | <u>0.20</u> | <u>1.16</u> |
| Depreciated value of plant and machinery [Rs.6.4 crores – Rs.1.16 crores] | | 5.24 |

Working Notes:

- (1)** As per section 352(iv), no depreciation shall be allowed in respect of plant and machinery purchased for scientific research relating to assessee's business, since the entire expenditure is deductible under section 35.
- (2)** No additional depreciation will be allowed on second hand plant and machinery as well as plant and machinery used for scientific research.

(3) Where an asset is acquired by the assessee during the previous year and is put to use for the purposes of business for a period of less than 180 days in that previous year, and the additional depreciation in respect of such asset is restricted to 10% of the actual cost for that previous year, then, the deduction for the balance additional depreciation i.e. 10% of the actual cost of such asset shall be allowed in the immediately succeeding previous year in respect of such asset.

Question 8: Computation of depreciation and additional depreciation: Venus Ltd., engaged in manufacture of pesticides, furnishes the following particulars relating to its manufacturing unit at Chennai (for the year ending 31-03-2023):

| | (Rs. In lacs) |
|-------------------------------------|---------------|
| Opening WDV of Plant and Machinery | 20 |
| New machinery purchased on 1-9-2022 | 10 |
| New car purchased on 1-12-2022 | 8 |
| Computer purchased on 3-1-2023 | 4 |

Additional information:

- All assets were put to use immediately.
- Computer has been installed in the office.
- During the year ended 31-3-2022, a new machinery had been purchased on 31-10-2021, for Rs.10 lacs. Additional depreciation, besides normal depreciation, had been claimed thereon.
- Depreciation rate of machinery may be taken as 15%.

Compute the depreciation available to the assessee as per the provisions of the income tax Act, 1961 and the WDV of different blocks of assets as on 31-3-2023. **(8 Marks, May 2016)**

Solution: Computation of depreciation and the WDV of different blocks of asset as on 31-03-2023

(amount in Rs.):

| Particulars | Block I (Plant & Machinery) & (Car) Block Rate 15% | Block II (Computer) Block Rate 40% |
|--|---|--|
| Opening WDV Opening WDV in case of car is Nil | 20,00,000 | Nil |
| Add: Assets acquired during the previous year (Rs.10,00,000 + Rs.8,00,000) (Computer Rs.4,00,000) | 18,00,000 | 4,00,000 |
| Less: Moneys payable in respect of assets sold during the year | Nil | Nil |
| WDV as on 31-3-2023 eligible for depreciation | 38,00,000 | 4,00,000 |
| Less: (a) Normal Depreciation - On car (Rs.8,00,000 x 75%, since used for less than 180 days and balance WDV i.e. Rs.30,00,000 x 15%) -- On computer (Rs.4,00,000 x 40% x 50%, since used for less than 180 days) | 5,10,000 | 80,000 |
| (b) Additional Depreciation - On plant (Rs.10,00,000 x 20%, since used for more than 180 days) [WN] | 2,00,000 | - |
| (c) Additional Depreciation - On plant (Rs.20,00,000 x 10%, since purchased in FY 2021-22 and put to use for less than 180 days) [WN] | 1,00,000 | - |
| WDV as on 14.2023 | 29,90,000 | 3,20,000 |

Working Notes:

1. In case of new machinery of Rs.20,00,000, additional depreciation is calculated @ 20% of actual cost since the asset is acquired during the previous year and put to use for a period of not less than 180 days.
2. Since the computer is installed in office building, the same shall not be eligible for additional depreciation.
3. Where an asset is acquired by the assessee during the previous year and is put to use for the purposes of business for a period of less than 180 day's in that previous year, and the additional depreciation in respect of such asset is restricted to 10% of the actual cost for that previous year, then, the deduction for the balance additional depreciation i.e. 10% of the actual cost of such asset shall be allowed in the immediately succeeding previous year in respect of such asset. Hence, on plant of Rs.10,00,000 which was purchased in FY 2021-22 and put to use for less than 180 days in that year, the remaining additional depreciation @ 10% is allowed in FY 2022-23.

Question 9: Computation of depreciation and additional depreciation: Gopichand Industries furnishes you the following information: (amount in Rs.)

| | |
|---|-----------|
| On 1-4-2022 - | |
| Block I: Plant and machinery (consisting of 10 looms) Rate of depreciation 15% WDV | 5,00,000 |
| Block II: Buildings (consisting of 3 buildings) Rate of depreciation 10% WDV | 12,50,000 |
| Acquired on 5-7-2022 -.5 looms for | 4,00,000 |
| Sold on 7-12-2022 -15 looms for | 10,00,000 |
| Acquired on 10-1-2023 – 2 looms for | 3,00,000 |

Compute depreciation claim.

Solution: Computation of depreciation claim (amount in ₹) -

| Particulars | Block I (Plant) | Block II (Buildings) |
|---|--------------------|-------------------------|
| Opening WDV | 5,00,000 | 12,50,000 |
| Add: Assets acquired during the previous year (Rs.4,00,000 + Rs.3,00,000) | 7,00,000 | — |
| | 12,00,000 | 12,50,000 |
| Less: Moneys payable in respect of assets sold during the year | 10,00,000 | — |
| WDV as on 31-3-2023 eligible for depreciation | 2,00,000 | 12,50,000 |
| Less: (a) Normal Depreciation (Rs.2,00,000 x 7.5%, since used for less than 180 days) | 15,000 | 1,25,000 |
| (b) Additional Depreciation (Rs.3,00,000 x 10%, since used for less than 180 days) [WN] | 30,000 | — |
| WDV as on 1-4-2023 | 1,55,000 | 11,25,000 |

Working Note: In case if plant is acquired during the year and is sold in the same year then no additional depreciation on the same shall be admissible. Hence, no additional depreciation can be claimed on 5 looms which were sold in the year of acquisition. The balance additional depreciation amounting 30,000 will be allowed in the immediately succeeding previous year.

No additional depreciation is admissible on building.

Question 10: Computation of depreciation and additional depreciation: Mr. Ravi is engaged in the business of generation and distribution of electric power'. He always opts to claim depreciation on written down value for income-tax purposes. From the following details, compute the depreciation allowable as per the provisions of the Income-tax Act, 1961 for the assessment year 2023-24: **(4 Marks, Nov. 2013)**

| | (in lacs) |
|--|-----------|
| (i) Opening WDV of block (15% rate) | 42 |
| (ii) New machinery purchased on 12-10-2022 | 10 |
| (iii) Machinery imported from Colombo on 12-04-2022. This machine had been used only in Colombo earlier and the assessee is the first user in India. | 9 |
| (iv) New computer installed in generation wing of the unit on 15-07-2022. | 2 |

Solution: Computation of depreciation (amount in Rs.):

| Particulars | Block I (Plant) Block Rate 15% | Block II (Computer) Block Rate 40% |
|---|-----------------------------------|--|
| Opening WDV | 42,00,000 | Nil |
| Add: Assets acquired during the previous year (Rs.10,00,000 + Rs.9,00,000) | 19,00,000 | 2,00,000 |
| Less: Moneys payable in respect of assets sold during the year | Nil | Nil |
| WDV as on 31-3-2023 eligible for depreciation | 61,00,000 | 2,00,000 |
| Less: (a) Normal Depreciation - On plant (Rs.10,00,000 x 7.5%, since used for less than 180 days and balance WDV i.e. Rs.51,00,000 x 15%) - On Computer (Rs.2,00,000 x 40%) | 8,40,000 | 80,000 |
| (b) Additional Depreciation - On plant (Rs.10,00,000 x 10%, since used for less than 180 days) — On computers (Rs.2,00,000 x 20%) [WN] | 1,00,000 | 40,000 |
| WDV as on 1-4-2023 | 51,60,000 | 80,000 |

Working Notes:

- (1) No Additional depreciation shall be allowed in respect of Machinery imported from Colombo which before its installation by the assessee, was used by any other person.
- (2) In case of new machinery of Rs.10,00,000, additional depreciation is calculated @ 10% of actual cost since the asset is acquired during the previous year and put to use for a period of less than 180 days. The balance additional depreciation amounting Rs.1,00,000 will be allowed in the immediately succeeding previous year.
- (3) Since the computer is installed in generation wing of the unit, the same shall be eligible for additional depreciation @ 20% i.e. Rs.2,00,000 x 20% = Rs.40,000.

Carry forward and setoff of unabsorbed depreciation

Unabsorbed depreciation [Section 32(2)]: The provisions relating to unabsorbed depreciation is as under—

1. Unabsorbed depreciation shall be allowed to be carried forward. It shall be treated as part of current year depreciation.
2. It can be carried forward whether or not the business or asset to which it relates is in existence.
3. Return of loss is not required to be submitted to carry forward unabsorbed depreciation.
4. Brought forward business losses (speculative or non speculative) under Section 72(2) and 73(3) shall be given priority of set off over unabsorbed depreciation.
5. Such unabsorbed depreciation can be carried forward for an indefinite period and set-off against any head of income (except Salaries).

DEPRECIATION IN CASE OF POWER GENERATING UNITS

Depreciation in case of Power Generating Unit [Section 32(1)(i)]:

The provisions relating to it are as follows —

- (1) **Applicability:** Section 32(1)(i) applies to an undertaking engaged in generation or generation and distribution of power i.e. it does not apply to an undertaking engaged in only distribution of power.
- (2) **Claim of depreciation on SLM basis instead of WDV:** These undertakings are given an option that, instead of Written Down Value method (WDV), they can claim the depreciation as per the Straight Line Method (SLM) on their individual assets. This option is to be exercised by the undertakings before due date of furnishing Return of Income under section 139(1) for the assessment year relevant to previous year in which they start generating power. Once exercised, the option shall be final and shall apply to subsequent assessment years.
- (3) **Treatment in case of sale of assets:** In case the tangible asset on which depreciation as per SLM is claimed, is sold, discarded, demolished or destroyed in any previous year (other than the year in which it is first put to use), then there can arise two situations which are as follows
 - (a) **Monies payable is less than WDV - Terminal depreciation [Section 32(1)(iii)]:** In case the Monies payable (including scrap) is less than the WDV of the asset, then such shortfall of monies payable over WDV shall be treated as 'Terminal Depreciation' under section 32(1)(iii), in the year in which such asset is so sold, discarded, demolished or destroyed.
 - (b) **Monies payable exceeds WDV - Balancing Charge [Section 41(2)]:** If the Moneys payable together with the scrap exceeds the WDV of the asset, then so much of the excess, as does not exceed the difference between the actual cost and the WDV, shall be treated as 'Balancing Charge' in the form of deemed business profits under section 41(2), in the year in which monies payable become due. Further, the excess of surplus over the actual cost is taxable as capital gains.
Balancing Charge = Lower of: (1) Actual cost - WDV of asset; or (2) Monies Payable — WDV of asset.
Capital Gains = Monies Payable — Actual Cost of the asset, if positive.
As per Explanation to Section 41(2): Where the monies payable become due in the previous year in which the business is no longer in existence, the provisions shall apply as if the business is in existence in that previous year.

Question 11: Balancing charge and terminal depreciation in case of power generating undertakings:

Determine the tax consequences in following cases for assessment year 2023-24

- (a) XYZ Co., an undertaking established in 2015 for generation and distribution of power, has opted for SLM method of depreciation. The written down value of its machinery as on 1-4-2022 was Rs.6,60,000. The machinery is sold for Rs.4,60,000 on 1-5-2022.

(b) ABC Co., a power-generating unit (opted for SLM), has purchased machinery on 1-5-2022 for Rs.10,00,000 which is destroyed by fire on 15-10-2022 and an insurance claim of Rs.8,80,000 is received on 31-1-2023.

(c) X A Co., an undertaking established in 2017 for generation of power, has opted for SLM method of depreciation. The company purchased a machinery for Rs.5,00,000. The written down value of its machinery as on 1-4-2022 is Rs.3,50,000. The machinery is sold for Rs.7,65,000 on 1-12-2022.

Solution The tax consequences in aforesaid cases shall be as follows —

(a) Here, monies payable is less than WDV, hence there shall be allowed deduction for terminal depreciation. Therefore, terminal Depreciation u/s 32(1)(iii) = Rs.6,60,000 — Rs.4,60,000 = Rs.2,00,000.

(b) Here, since machine is destroyed in the same previous year in which it is first put to use, hence there is no terminal depreciation. The amount of loss, to the extent not reimbursed by insurance company, shall be treated as Short- Term Capital Loss. Therefore, STCL = Rs.10,00,000 — Rs.8,80,000 = Rs.1,20,000.

(c) Here, monies payable is greater than WDV.

Therefore, Balancing Charge u/s 41(2) = [(Lower of Rs.5,00,000 or Rs.7,65,000) — Rs.3,50,000] = Rs.1,50,000; and Short-Term Capital Gains = Rs.7,65,000 — Rs.5,00,000 = Rs.2,65,000.

CERTAIN SPECIAL DEDUCTIONS - SECTION 35 TO 35DDA

Deductions available in respect of expenditure incurred on 'Scientific Research' [Section 35]:

(1) Meaning of Scientific research As per Section 43(4), 'Scientific research means any activities for the extension of knowledge in the fields of natural or applied science including agriculture, animal husbandry or fisheries.

(2) Deduction in relation to expenditure incurred on scientific research [Section 35]

| Section 35 | Expenditure incurred | Amt. of deduction | Conditions / Remarks |
|---------------|---|--------------------------------|---|
| (1)(i) | <ul style="list-style-type: none"> ➤ Revenue expenditure on scientific research related to business. ➤ Expenditure on scientific research before commencement of business by way of — <ul style="list-style-type: none"> (a) Purchase of materials; or (b) Salary (other than perquisite) of employees | Amount of expenditure incurred | Expenditure incurred within 3 years immediately preceding commencement of business is allowed as deduction in the year of commencement of business to the extent certified by the prescribed authority. |
| (1) (iv)/ (2) | <ul style="list-style-type: none"> ➤ Sum paid to a research association, university, college or institution whose object is undertaking of scientific research** | Sum so paid | <ul style="list-style-type: none"> ➤ **Such association, university college or institution must be approved as per prescribed guidelines and must be notified by the Central Government. |

| | | | |
|---------------------------------|--|--------------------------------|--|
| | | | <ul style="list-style-type: none"> ➤ Deduction is allowed even if research is not related to business. |
| (1)(iia) | <ul style="list-style-type: none"> ➤ Sum paid to a company having as its main object 'scientific research and development' to be used by it for scientific research | Sum so paid | Such company is registered in India, is approved by prescribed authority and fulfils other prescribed conditions. |
| (1)(iv)/ (2)(i)(iii) | <ul style="list-style-type: none"> ➤ Sum paid for social science or statistical research to a research association which has as its object the undertaking of research in social science or statistical research or to a university, college, or institutions* <p>(See Note 1)</p> | Sum so paid | <ul style="list-style-type: none"> ➤ Such association, university college or institution must be approved as per prescribed guidelines and must be notified by the Central Government. ➤ Deduction is allowed even if research is not related to business. |
| (1)(iv)/ (2) | <ul style="list-style-type: none"> ➤ Capital expenditure (except expenditure on the purchase of land on scientific research related to business, ➤ Capital expenditure (except expenditure on the purchase of land) incurred before the commencement of business. | Amount of expenditure incurred | <ul style="list-style-type: none"> ➤ Expenditure incurred within 3 years immediately preceding the commencement of business is allowed in the year of the commencement of the business. ➤ No depreciation is allowable. |
| (2AA) | <ul style="list-style-type: none"> ➤ Sum paid to - <ul style="list-style-type: none"> (a) a National Laboratory; or (b) a University; or (c) an Indian Institute of technology; or (d) a specified person (See Note 11 | Sum so paid | <ul style="list-style-type: none"> ➤ Sum is paid with a specific direction that it shall be used for scientific research undertaken under a programme approved in this behalf by prescribed authority. ➤ No deduction shall be allowed in respect of such sum under any other provision of the Act. ➤ The prescribed authority shall, before granting approval, satisfy itself about the feasibility of carrying out the scientific research and shall submit its report to the |

| | | | |
|--------------|---|--------------------------------|--|
| | | | Principal (Thief Commissioner or Chief (Commissioner or Principal Director General or Director General in such form as may be prescribed. |
| (2AB) | <ul style="list-style-type: none"> ➤ *Expenditure (not being in nature of cost of any land or buildings incurred on in-house research and development facility incurred by a company engaged in the business of biotechnology, or, arty business of manufacture or production of any article or thing, not being an article or thing specified in the list of the Eleventh Schedule. ➤ Expenditure on scientific research in relation to drugs and pharmaceuticals includes expenditure on clinical drug trial, obtaining approval from any regulatory authority and filing a t application for patent. | Amount of expenditure incurred | <ul style="list-style-type: none"> ➤ Such Research and development facility is approved by prescribed authority. ➤ Such assessee should enter into an agreement with prescribed authority for co-operation in such Research and development facility and fulfils such conditions with regard to maintenance of accounts and audit thereof and furnishing of reports in such manner as may be prescribed. ➤ The prescribed authority shall submit its report in relation to the approval of the said facility to the Principal Chief Commissioner or Chief Commissioner or Principal Director General or Director General in such form and within such time as may he prescribed. ➤ No deduction shall be allowed in respect of such sum under any other provision of the Act. ➤ No deduction shall be allowed in this sub-section to a company approved under section 35(1)(iia). |

Notes:

(1) Deduction not to he denied even if approval withdrawn subsequently The deduction allowable under this section shall not be denied merely on the ground that subsequent to the payment of such sum by the assessee,

(a) the approval granted to association, university, college, other institution referred to u/s 35(1)(ii)/ (iii), or the company referred u/s 35(1)(iia) or the Laboratory or specified person referred to under section 35(2AA) has been withdrawn; or

(b) the approval granted to the programme undertaken by the National Laboratory, University, Indian Institute of Technology or specified person, has been withdrawn.

(2) Intimation to prescribed income tax authority within 3 months Every notification for approval under Section 35(i)(ii)/(iia/ (iii) in respect of the research association, university, college or other institution or the company issued on or before 01-04-2022, shall be deemed to have been withdrawn unless such research association, university, college or other institution or company makes an intimation in prescribed form and manner to the prescribed income--tax authority within 3 months from 01-04-2022, and subject to such intimation the notification shall be valid for a period of 5 consecutive assessment years beginning with the assessment year commencing on or after 01 -04-2023.

Notification to be effective for a period not exceeding 5 years Any notification issued by the Central Government any one time, have effect for such assessment year or years, not exceeding 5 assessment years as may he specified in the notification.

(3) **Conditions for claiming deduction:** The research association, university, college or other institution or company referred to in Section 35(1)(ii)/(iia)/(iii) shall not be entitled to deduction, unless such research association, university, college or other institution or company—

(i) **Prescribed statement to be furnished:** Prepares prescribed statement for prescribed period in prescribed form and delivers the said statement to prescribed income-tax authority or authorized person by such authority:

Correction statement to be furnished: Such research association, university, college or other institution or the company may also deliver to the prescribed authority a correction statement for rectification of any mistake or to add, delete or update the information furnished in the statement delivered in such form and verified in such manner as may be prescribed; and

(ii) **Certificate to be furnished to the donor:** Furnishes to the donor, a certificate specifying the amount of donation in such manner, containing such particulars and within such time from the date of receipt of sum, as may be prescribed.

(4) Expenditure incurred on scientific research includes all expenditure incurred for the prosecution, or the provision of facilities for the prosecution, of scientific research, but do not include any expenditure incurred in the acquisition of rights in, or arising out of, scientific research.

(5) Research related to business or class of business includes —

(a) Any scientific research which may lead to or facilitate an extension of that business or, as the case may he, all business of that class.

(b) Any scientific research of a medical nature, which has a special relation to the welfare of workers, employed in that business / all businesses of that class.

(6) According to Section 35(4) unabsorbed scientific research capital expenditure is carried forward and set-off in the same manner as unabsorbed depreciation.

(3) **Actual use for scientific research during the previous year — Not necessary:** Deduction under section 35(1)(iv) is available only If the asset was acquired during the previous year for the purposes of scientific research. There is no further requirement that asset must be put to use in the relevant previous year.

Tax treatment in case the asset acquired for scientific research is sold during the year

Tax treatment in case of sale of scientific research assets is as under —

- (1) When the asset is sold without being used for other purposes: In such a case, there shall be deemed profits in the year in which sale takes place.
 - (i) The taxable amount under section 41(3) shall be = So much of the sale proceeds which do not exceed the amount of deduction allowed under section 35.
 - (ii) Capital gains under section 45 Excess of sale proceeds over the cost of acquisition and expenditure incurred on transfer.
- (2) When the asset is sold after being used for business purposes : In such a case, treatment will be as follows -
 - (i) At the time of use for business purposes: The cost of such asset will be added to the WDV of relevant block. As per Section 43(1), the cost of such asset will be Actual cost of the asset less Deduction allowed under section 35(2) i.e. cost will be NIL as 100% deduction was allowed under section 35(2).
 - (ii) At the time of sale: When the asset is sold, the treatment is done as if an asset forming part of block is sold. Capital gains arising are to be computed under Section 50.

Question 12: Expenditure on Scientific research: Mr. Praveen Kumar has furnished the following particulars relating to payments made towards scientific research for the year ended 31-3-2023

| | (in lacs) |
|--|-----------|
| (i) Payments made to K Research Ltd. | 20 |
| (ii) Payment made to LMN College | 15 |
| (iii) Payment made to OPQ College. | 10 |
| Note: K Research Ltd. and LMN College are approved research institutions and these payments are to be used for the purposes of scientific research. | |
| (iv) Payment made to National Laboratory | 8 |
| (v) Machinery purchased for in-house scientific research | 25 |
| (vi) Salaries to research staff engaged in in-house scientific research | 12 |

Compute the amount of deduction available under section 35. (4 Marks, IPCC May 2011).

Solution: Computation of deduction under section 35 of the Act (amount in) -

| Particulars | Section | Qualifying Sum | Deduction |
|--|-----------|----------------|------------------|
| (i) Payments made to K Research Ltd.(approved company,) [WN-1] | 35(1)(ia) | 20,00,000 | 20,00,000 |
| (ii) Payment made to LMN College approved institution | 35(1)(ii) | 15,00,000 | 15,00,000 |
| (iii) Payment made to OPQ College [WN-2] | 35(2AA) | - | - |
| (iv) Payment to National Laboratory [WN-3] | 35(1)(iv) | 8,00,000 | 8,00,000 |
| (v) Machinery purchased for in-house scientific research [WN-4] | 35(1)(i) | 25,00,000 | 25,00,000 |
| (vi) Salaries to research staff engaged in in-house scientific research [WN-5] | | 12,00,000 | 12,00,000 |
| Total Deduction | | | 80,00,000 |

Working Notes:

- (1) Payments made to K research Ltd. an Indian company shall be eligible for deduction of 100% u/s 35(i)(iia).
- (2) Since in the question it has been specifically provided that K Research Ltd. and LMN College are approved, hence it can be concluded that OPQ College is not an approved research institution. Therefore payment made to OPQ college shall not be eligible for deduction.
- (3) Payment to National Laboratory is eligible for deduction under section 35(2AA) @ 100% of the sum so paid.
- (4) Mr. Praveen Kumar is an individual shall not be eligible for deduction of 100% for in house research under section 35(2AB) since the same is available only to a company assessee.
- (5) Salaries to research staff engaged in in-house scientific research is not eligible for deduction under section 35(2A13) as the said deduction is available only to a company assessee.

Question 13: Expenditure on Scientific research: vitha Bio-medicals Ltd. is engaged in the business of manufacture of bio-medical items. The following expenses were incurred in respect of activities connected with scientific research:

| Year ended | Item | Rs. |
|---------------------------|----------------------------|-----------|
| 30-12-2020 | Land | 10,00,000 |
| (incurred after 1-9-2019) | Building | 25,00,000 |
| 31-03-2021 | Plant and machinery | 5,00,000 |
| 31-03-2022 | Raw materials | 2,20,000 |
| 31-03-2023 | Raw materials and salaries | 1,80,000 |

The business was commenced on 01-09-2022 In view of availability of better model plant and machinery, the existing plant and machinery were sold for Rs.8,00,000 on 01-03-2023.

Discuss the implications of the above for assessment year 2023-24 along with brief computation of deduction permissible under section 35, assuming that necessary conditions have been fulfilled.

(7 Marks, PCE Nov. 2007)

Solution: Expenditure incurred other than cost of land or building) on in-house research and development facility as approved by the prescribed authority, by a company engaged in the business of bio-technology shall be allowed as deduction to the extent of 100% of such expenditure under section 35(2AB).

Expenditure incurred within the 3 years preceding the date in which the business commences, on salary paid to an employee engaged in such scientific research or on the purchase of materials used in such scientific research, or capital expenditure (other than cost of land), shall be allowed as deduction, to the extent of 100% of such expenditure (allowed in the previous year i.e. year of commencement of business). The relevant computation is as under —

➤ **Computation of amount of deduction under section 35 (amounts in Rs.)**

| Particulars | Expenditure allowable u/s 35(1)(i) and (iv) at 100% | Expenditure allowable u/s 35(2AB) at 100% |
|-------------|---|---|
| Land | - | - |
| Building | 25,00,000 | - |

| | | |
|---|------------------|------------------|
| Plant and machinery | 5,00,000 | - |
| Raw material | 2,22,000 | - |
| Raw material and salaries | - | 1,80,000 |
| Eligible expenditure | 32,20,000 | 1,80,000 |
| Deduction allowable | 32,20,000 | 1,80,000 |
| Total deduction allowable u/s 35 | | 34,00,000 |

➤ When the asset is sold without being used for other purposes: In such a case, there shall be deemed profits in the year in which sale took place.

(a) The taxable amount under section 41(3) shall be = So much of the sale proceeds which do not exceed the amount of deduction allowed under section 35 i.e. Rs.5 lakhs.

(b) Capital gains under section 45= Excess of sale proceeds over the cost of acquisition and expenditure incurred on transfer. Short-term capital gains = Moneys payable — Cost = Rs.8 lakhs - Rs.5 lakhs = Rs.3 lakhs.

Deduction in respect of expenditure on Specified Business [Section 35AD]

1. **Optional deduction:** An assessee shall be allowed deduction under this section if he opts for the provisions of this section.

2. **Meaning of Specified business:** Specified business means any one or more of the following business namely:

(a) **Cold chain facilities:** Setting up and operating cold chain facilities for specified products, if its operations are commenced on or after 1-4-2009;

(b) **Warehousing facilities-Agricultural produce:** Setting up and operating warehousing facilities for storing agricultural produce, if its operations are commenced on or after 1-4-2009;

(c) **Hospitals:** Building and operating, anywhere in India, a hospital with at least one hundred beds for patients, if its operations are commenced on or after 1-4-2010;

(d) **Housing Projects:** Developing and building a housing project under a notified scheme for affordable housing framed by the Central Government or a State Government, as the case may be, and notified by the CBDT in this behalf in accordance with the guidelines as may be prescribed, if its operations are commenced on or after 1-4-2011;

(e) **Fertilizer plant:** Production of fertilizer in India in a new plant or in a newly installed capacity in an existing plant if its operations are commenced on or after 1-4-2011;

(f) **Cross-country natural gas pipeline network:** Laying & operating a cross-country natural gas pipeline network for distribution, including storage facilities being an integral part of such network, if its operations are commenced on or after 1-4-2007;

(g) **Cross-country crude or petroleum oil pipeline network:** Laying and operating a cross-country crude or petroleum oil pipeline network for distribution, including storage facilities being an integral part of such network, if its operations are commenced on or after 1-4-2009;

(h) **Hotel:** Building and operating, anywhere in India, a hotel of two star or above category as classified by Central government, if its operations are commenced on or after the 1-4-2010;

- (i) **Slum redevelopment housing project:** Developing and building a housing project under a scheme for slum redevelopment or rehabilitation framed by the Central Government or a State Government, as the case may be, and notified by the CBDT in accordance with the prescribed guidelines, if its operations are commenced on or after 1-4-2010;
- (j) **ICD/CFS:** Setting up and operating an inland container depot or a container freight station notified or approved under the customs Act, 1962, if its operations are commenced on or after 1-4-2012;
- (k) **Bee-keeping and production of honey and beeswax:** Bee-keeping and production of honey and beeswax, if its operations are commenced on or after 1-4-2012;
- (l) **Warehousing facilities-Sugar:** Setting up and operating a warehousing facility for storage of sugar, if its operations are commenced on or after 1-4-2012.
- (m) **Slurry pipe line:** Laying and operating a slurry pipeline for transportation of iron ore on or after 1-4-2014.
- (n) **Semi-conductor wafer fabrication manufacturing unit:** Setting up and operating a semi-conductor wafer fabrication manufacturing unit on or after 1-4-2014.
- (o) **Infrastructure facility:** Developing or maintaining and operating or developing, maintaining and operating a new infrastructure facility on or after 01-04-2017.

3. Eligible deduction: 100% of the capital expenditure incurred, wholly and exclusively, for the purposes of any specified business carried on by the assessee shall be allowed as deduction during the previous year in which such expenditure is incurred by him.

Deduction in respect of expenditure incurred prior to commencement: Further, the expenditure incurred, wholly and exclusively, for any specified business, shall be allowed as deduction during the previous year in which he commences operations of his specified business, if —

- (a) the expenditure is incurred prior to the commencement of its operations; a
- (b) the amount is capitalised in the books of account of the assessee on the date of commencement of its operations.

Cash expenditure exceeding Rs.10,000 or expenditure on land, goodwill and financial instrument not eligible:

Any expenditure of capital nature shall not include any expenditure in respect of which the payment or aggregate of payments made to a person in a day, otherwise than by an account payee cheque drawn on a bank or an account payee bank draft or use of electronic clearing system through a bank account, or through such other electronic mode as may be prescribed, exceeds Rs.10,000 or any expenditure incurred on the acquisition of any land or goodwill or financial instrument. [(a) Credit Card; (b) Debit Card; (c) Net Banking; (d) IMPS (Immediate Payment Service); (e) UPI (Unified Payment Interface); (f) RTGS (Real Time Gross Settlement.); (g) NEFT (National Electronic Funds Transfer), and (h) BHIM (Bharat interface for Money) Aadhar Pay have been prescribed as mode of electronic payment.

4. Conditions to be fulfilled in respect of specified business in order to claim deduction: the specified business must fulfill the following conditions namely

- (a) it is not set up by splitting up, or the reconstruction, of a business already in existence; or

- (b) it is not set up by the transfer of plant or machinery previously used for any purpose. However, where —
- (i) the value of second hand plant and machinery doesn't exceed 20% of total value of plant or machinery used in that business, or
 - (ii) such second hand machinery is the one imported by the assessee on which no depreciation was allowed or allowable under this Act in any other earlier year,
- then, this condition is not violated.

5. Minimum use of capital asset for specified business - 8 years: Any asset in respect of which a deduction is claimed and allowed under this section shall be used only for the specified business, for a period of eight years beginning with the previous year in which such asset is acquired or constructed.

6. Assets used for purposes other than specified business Consequences thereof: Where any asset, in respect of which a deduction is claimed and allowed under this section, is used for a purpose other than the specified business during the period of 8 years, otherwise than by way of a mode referred to in section 28(vii), the total amount of deduction so claimed and allowed in one or more previous years, as reduced by the amount of depreciation allowable in accordance with the provisions of section 32, as if no deduction under this section was allowed, shall be deemed to be the income of the assessee chargeable under the head "Profits and gains of business or profession" of the previous year in which the asset is so used.

However, above provision shall not apply to a company which has become a sick industrial company u/s 17(1) of the Sick Industrial Companies (Special Provisions) Act, 1985, during the period of 8 years as specified above.

7. Owner of a hotel eligible for deduction even if he transfers the operation of the hotel to another person: The assessee shall be deemed to be carrying on the specified business of building and operating hotel if—

- (a) the assessee builds a hotel of two-star or above category;
- (b) thereafter, he transfers the operation of the hotel to another person;
- (c) he, however, should continue to own the hotel.

8. Deduction allowed under this section, not to be claimed under any other provision:

- (a) Where a deduction under this section is claimed and allowed in respect of the specified business for any assessment year, no deduction shall be allowed under the provisions (if Chapter VI-A i.e. section 80-IA to 80-RRB or Section 10AA in relation to such specified business for the same or any other assessment year.
- (b) No deduction in respect of the expenditure shall be allowed to the assessee under any other section in any previous year or under this section in any other previous year, if the deduction has been claimed or opted by the assessee and allowed to him under this section.

9. Certain provisions to apply: the provisions contained in Section 80A(6), 80-IA(7) and 80-IA(10) shall, so far as may be, apply to this section in respect of goods or services or assets held for the purposes of the specified business.

10. Carry forward and set off loss from specified business: As per Section 73A, loss from specified business can be carried forward and set off only from profits of specified business. Such loss can, however, be carried forward indefinitely for set-off against profits of the same or any other specified business but the assessee has to file return of income on or before the due date of filing return of income under section 139 for carry forward of losses from specified business.

11. Meaning of Cold chain facility: It means a chain of facilities for storage or transportation of agricultural and forest produce, meat and meat products, poultry, marine and dairy products, products of horticulture, floriculture and apiculture and processed food items under scientifically controlled conditions including refrigeration and other facilities necessary for preservation of such produce.

Question 14: Deduction of expenditure on Specified Business u/s 35AD: Win Limited commenced the business of operating a three star hotel in Tirupati on 1-4-2022.

- (i) Cost of land (acquired in June 2020) Rs.60 lakhs
 - (ii) Cost of construction of hotel building
 - Financial year 2021-22 Rs.30 lakhs
 - Financial year 2022-23 Rs.150 lakhs

[Out of expenditure of Rs.150 lakhs, Rs.1,50,000 is paid in cash to contractor on 10-09-2022 and Rs.50,000 is paid in cash of 15-01-2023 and balance through a account payee cheque]
 - (iii) Plant and Machinery (all new) acquired during financial year 2022-23 Rs.30 lakhs
- [All the above expenditures were capitalized in the books of the company]
- “Net profit before depreciation for the financial year 2022-23 Rs.80 lakhs

Determine the amount eligible for deduction u/s 35AD of the Income tax Act for AY 2023-24,

(4 Marks, PCC May 2011)

Solution: Computation of amount eligible for deduction u/s 35AD: As per Section 35AD in case an assessee is engaged in the business of operating a hotel of 2-star or above category (i.e., 3-star category) on or after 1-4-2010, it is eligible for deduction under section 35AD. Since Win Ltd. is engaged in the business of operating a hotel of 3-star category, hence, it is eligible for deduction under section 35AD. Deduction shall be allowed in respect of the capital expenditure incurred in the earlier years (i.e. years earlier than the previous year 2022-23, as the expenditure has been capitalized in the books of accounts in the current financial year; and the expenditure incurred in the previous year.

Any expenditure of capital nature shall not include any expenditure in respect of which the payment or aggregate of payments made to a person in a day, otherwise than by an account payee cheque drawn on a bank or an account payee bank draft or use of electronic clearing system through a bank account or through such other electronic mode as may be prescribed, exceeds Rs.10,000 or any expenditure incurred on the acquisition of any land or goodwill or financial instrument.

The relevant computations are (Rs. in lakhs)

| | | |
|--|------|----|
| Net profit before depreciation for the financial year 2022-23 | | 80 |
| Less: Deduction u/s 35AD | | |
| Cost of construction of hotel building (Rs.148 + Rs.30) (Rs.1.5 and Rs.0.5 lakhs shall not be eligible for deduction since the same is paid in cash) | -178 | |

| | | |
|--|-----|------|
| Plant and Machinery (all new) acquired during financial year 2022-23 | -30 | -208 |
| Loss to be carried forward under section 73A for indefinite period (to be set-off only against business specified in section 35AD) | | -128 |

Question: 15— Consequences of misutilisation of asset whose deduction is claimed in 35AD: XYZ Ltd commenced business of production of fertilizer on 1-4-2020. The company purchased plant and machinery of the fertilizer amounting Rs.100 lakhs for which deduction was claimed under Section 35AD in financial year 2022-23 the said asset was used for non-specified business. You are required to determine the tax implications of the said transaction in hands of XYZ Ltd.

Solution: According to Section 35AD(7B), if any asset is used for any purpose other than the specified business, the total amount of deduction so claimed and allowed in any previous year in respect of such asset, as reduced by the amount of depreciation allowable in accordance with the provisions of section 32 as if no deduction had been allowed under section 35AD, shall be deemed to be income of the assessee chargeable under the head “Profits and gains of business or profession” of the previous year in which the asset is so used. Hence, the relevant computation will be as under: (Rs. in lakhs)

| | |
|---|-------|
| Total amount of deduction claimed and allowed in respect of such asset u/s 35AD | 100 |
| Less: Depreciation eligible under Section 32 in respect of such asset [WN] | 44.75 |
| Deemed profits u/s 35AD | 55.25 |
| Actual Cost of asset | 100 |
| Less: Depreciation eligible under Section 32 (including additional depreciation) for FY 2020-2Q | 35 |
| WDV | 65 |
| Less: Depreciation eligible under Section 32 for FY 2021-22 | 9.75 |
| WDV as on 01-04-2022 | 55.25 |
| Deduction admissible on account of depreciation for FY 2020 – 21 and 2021 – 22 | 44.75 |

Expenditure by way of payment to associations and institutions for carrying out Rural Development Programmes [Section 35CCA]:

(1) Eligible payments: Where an assessee incurs any expenditure by way of payment of any sum -
(a) to a rural development fund set up and notified by the Central Government in this behalf; or
(b) to the National Urban Poverty Eradication Fund set up and notified by the Central Government in this behalf,
the assessee shall, subject to the provisions of this section, be allowed a deduction of the amount of such expenditure incurred during the previous year.

(2) No double deduction: Where a deduction under this section has been claimed and allowed in respect of any expenditure, no deduction shall be allowed in respect of such expenditure under any other provision of the Act for the same or any other assessment year.

Expenditure incurred on notified Agricultural Extension Project [Section 35CCC]: The provisions relating to this section are -

1) Nature of expenditure: Any expenditure on notified agricultural extension project in accordance with the prescribed guidelines.

2) Amount of deduction: 100% of such expenditure.

3) No double deduction: Where a deduction under this section is claimed and allowed for any assessment year in respect (31 any expenditure, deduction shall not be allowed in respect of such expenditure under any other provisions of this Act for the same or any other assessment year.

Provisions relating to the expenditure incurred by companies on notified skill development project.

Expenditure incurred by companies on notified Skill Development Project [Section 35CCD1: The provisions relating to this section are —

(1) Eligible Assessee: Company Assessee.

(2) Nature of expenditure: Any expenditure (not being expenditure in the nature of cost of any land or building) on any notified Skill Development Project in accordance with prescribed guidelines.

(3) Amount of deduction: 100% of such expenditure.

(4) No double deduction: Where a deduction under this section is claimed and allowed for any assessment year in respect of any expenditure, deduction shall not be allowed in respect of such expenditure under any other provisions of this Act for the same or any other assessment year.

Question 16: Computation of “Profits and gains of business or profession: Isac limited is a company engaged in the business of biotechnology. The net profit of the company for the financial year ended 31-03-2023 is Rs.15,25,890 after debiting the following items

| | Particulars | Rs. |
|----|---|----------|
| 1) | Purchase price of raw material used for the purpose of in-house research and development | 1,80,000 |
| 2) | Purchase price of asset used for in house research and development wrongly debited to profit and loss account | |
| | (a) Land | 5,00,000 |
| | (b) Building | 3,00,000 |
| 3) | Expenditure incurred on notified agricultural extension project | 1,50,000 |
| 4) | Expenditure on notified skill development project | |
| | (a) Purchase of land | 2,00,000 |
| | (b) Expenditure on training for skill development | 2,50,000 |
| 5) | Expenditure on training for skill development .Expenditure incurred on advertisement ‘in ‘the souvenir published by a political party | 75,000 |

Compute the income under the head “Profits and gains of business or profession” for the A.Y. 2023-24 of Isac Ltd.

Solution: Computation of income under the head ‘Profits and gains of business or profession” for the A.Y. 2023-24:

| Particulars | Rs. | Rs. |
|---|-----|-----------|
| Net profit as per Profit and Loss A/c | | 15,25,890 |
| Add: Items debited to P&L A/c, but to be disallowed - | | |
| Purchase price of raw material used for in-house research and development | - | |

| | | |
|--|----------|------------------|
| [WN-1] | | |
| Purchase price of land used in in-house research and development [WN-2] | 5,00,000 | |
| Purchase price of building used in in-house research and development WN-3] | - | |
| Expenditure incurred on notified agricultural extension project [WN-4] | - | |
| Expenditure incurred on purchase of land for notified skill development project [WN-5] | 2,00,000 | |
| Expenditure incurred on training for skill development for notified skill development project [WN-6] | - | |
| Expenditure incurred on advertisement in the souvenir published by a political party [WN-7] | 75,000 | 7,75,000 |
| Profit and gains from business | | 23,00,890 |

Working Notes:

- (1) Purchase price of raw material used for the purpose of in-house research and development — 100% deduction is admissible. Since the same is already debited to P & L A/c hence no adjustment is required.
- (2) Purchase price of land is not allowable as deduction under section 35(2AB).
- (3) Cost of building, being capital expenditure, 100% deduction shall be allowed u/s 35(1)(iv) read with section 35(2). Since [lie same is already debited to P & L A/c hence no adjustment is required.
- (4) This expenditure qualifies for 100% deduction under section 35CCC. Since the same is already debited to P & L A/c hence no adjustment is required.
- (5) Purchase of land does not qualify for deduction under section 35CCD.
- (6) This expenditure qualifies for 100% deduction under section 35CCD. Since the same is already debited to P & L A/c hence no adjustment is required.
- (7) The expenditure incurred on advertisement in the souvenir published by a political party is disallowed as per section 37(211) while computing income under the head “Profit and Gains of Business or Profession” but the same would be allowed as deduction under section 80GGB from the gross total income of the company.

Deduction relating to preliminary expenses.

Amortization of certain Preliminary Expenses [Section 35D]:

- 1) **Eligible Assessee:** Indian Company or a person (other than a company) resident in India.
- 2) **Deduction to be allowed in 5 equal installment:** Where an eligible assessee incurs any expenditure on preliminary expenses,—
 - (a) before the commencement of his business; or
 - (b) after the commencement of his business, in connection with the extension of his undertaking or in connection with his setting up a new unit;

he shall be allowed a deduction of an amount equal to $1/5^{\text{th}}$ of such expenditure for each of the 5 successive previous years beginning with the previous year in which the business commences, or the previous year in which the extension of the undertaking is completed or the new unit commences production or operation.

3) Expenditure eligible for deduction: Expenditure eligible for deduction shall be.-

- (a) Expenditure in connection with -
 - (i) preparation of feasibility report;
 - (ii) preparation of project report;
 - (iii) conducting market or any other survey necessary for business of the assessee; or
 - (iv) Engineering services relating to the business of the assessee.
- (b) Legal charges for drafting any agreement between the assessee and any other person for any purpose relating to the setting up or conduct of the business of the assessee.
- (c) Where the assessee is a company, also expenditure of —
 - (i) Legal charges for drafting its Memorandum and Articles of Association; or
 - (ii) Printing charges of its Memorandum and Articles of Association; or
 - (iii) Registration fees for its registration under the provisions of the companies Act 1956; or
 - (iv) Underwriting commission, brokerage and charges for drafting, typing, printing and advertisement of the prospectus, in connection with the issue of shares or debentures of the company for public subscription;
- (d) Such other expenditure, not being eligible for any allowance or deduction under any other provisions of the Act, as may be prescribed

4) Amount qualifying for deduction: Lower of the following qualifies for deduction

- (a) Aggregate amount of eligible expenditure; or
- (b) Higher of (i) or (ii)
 - (i) 5% of Cost of the project; or
 - (ii) 5% of Capital employed (Only in the case of an Indian company).
 - “Cost of project” means actual cost of fixed assets acquired or developed in relation to such commencement, extension or set up, a or which are shown as on 31st March of relevant previous year.
 - “Capital employed in the business of company” means — [issued share capital + debentures + Long-Term borrowings] in relation to such commencement, extension or set up and which are shown as on 31st March of the relevant previous year.

Note: “Relevant previous year” means the year in which the business is commenced; or the extension of such industrial undertaking is completed; or the new industrial unit commences production or operation.

5) Audit of accounts : Where the assessee is a person other than a company or a co-operative society, no deduction shall be admissible unless the accounts of the assessee for the year or years in which the expenditure is incurred have been audited by a Chartered accountant before the specified date referred to in section 44AB (i.e., one month prior to the due date for furnishing return of income u/s 139(1)) and the assessee furnishes for the first year in which the deduction under this section is claimed, the report of such audit by that date in the prescribed form duly signed and verified by such accountant and setting forth such particulars as may be prescribed.

6) Transfer of undertaking in scheme of amalgamation demerger: Where the undertaking of an Indian company entitled to deduction under this section is transferred, before the expiry of the period of 5 years, to another Indian company in a scheme of amalgamation/ demerger, then -

- (i) no deduction shall be admissible in the case of the amalgamating / demerged company for the previous year in which the amalgamation / demerger takes place; and
- (ii) the provisions of this section shall apply to the amalgamated/resulting company, as they would have applied to the amalgamating / demerged company, if the amalgamation/demerger had not taken place.

7) No double deduction: Where a deduction under this section is claimed and allowed in respect of any expenditure, the expenditure in respect of which deduction is so allowed shall not qualify for deduction under any other provision of this Act for the same or any other assessment year.

8) Service units eligible: Deduction under this section is available to all undertakings including service sector units as well.

Question 17:Jardine Ltd., is an existing Indian Company, which sets up a new industrial unit. It incurs the following expenditure in connection with the new unit **(Amounts in Rs.)**

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

What is the deduction admissible to the company under section 35D?

What will be your answer if the above facts relate to Mr. Jardine, a resident in India?

Solution: In case of Jardine Ltd.: In case of an Indian company, the preliminary expenditure qualifying for deduction cannot exceed higher of the following two limits,

- (i) 5% of cost of project i.e. 5% of 30,00,000 i.e. Rs.1,50,000, or
- (ii) 5% of capital employed i.e. 5% of Rs.40,00,000 i.e. Rs.2,00,000,

Therefore, the qualifying amount for deduction = Rs.2,00,000, which shall be allowed in five equal annual instalments of Rs.40,000 each beginning with previous year in which new industrial unit is set up.

In case of Mr. Jardine: It must be noted that the option of 5% of capital employed is available only in case of Indian company. Therefore, in case of Mr. Jardine, the qualifying amount of deduction = 5% of 30,00,000 i.e. Rs.1,50,000, which shall be allowed in five equal annual installments of Rs.30,000 each.

Amortization of expenditure incurred under Voluntary Retirement Scheme [Section 35DDA]:

The provisions relating to this section are —

- 1) **Eligible Assessee:** Any person.
- 2) **Eligible expenditure:** 100% of expenditure incurred by an assessee in any previous year by way of payment of any sum to an employee in connection with his voluntary retirement in accordance with any scheme(s).

- 3) Deduction and Period:** 1/5th of such expenditure is deductible for each of 5 successive previous years starting with the previous year in which such expenditure is incurred.
- 4) Transfer of undertaking in scheme of amalgamation demerger:** Where the assessee, being an Indian company, is entitled to the deduction under the said section and the undertaking of such company is transferred, before the expiry of the period as specified, to another Indian company in a scheme of amalgamation / demerger, then no deduction shall be allowed to the amalgamating / demerged company and the provisions shall apply to the amalgamated/demerged company, as they would have applied to the amalgamating / demerged company, if the amalgamation/ demerger had not taken place.
- 5) Transfer of undertaking in scheme of business reorganisation:** Where there has been reorganisation of business, whereby a firm is succeeded by a company fulfilling the conditions as specified in Section 47(xiii), or a proprietary concern is succeeded by a company fulfilling the conditions as specified in Section 47(xiv) or unlisted company or private company is converted into Limited liability partnership fulfilling the conditions of 47(xiiib), then the provisions of this section shall apply to the successor company or limited liability partnership, as they would have applied to the firm or the proprietary concern or unlisted company or private company, if reorganisation of business had not taken place.
- 6) No double deduction:** No deduction shall be allowed in respect of such expenditure incurred under any other provision of this Act.

Various deductions allowable under Section 36(1)

Other Deductions [Section 36]: In the computing the income referred to in section 28, the deductions provided for in the following clauses of section 36(1) shall be allowed in respect of the matters dealt with therein —

| S 36(1) | Deductible Expenditure | Conditions/ Remarks |
|---------|--|---|
| (i) | ➤ Insurance premium of stock or stores against damage or destruction thereof. | ➤ Such stock or stores are used for Business or Profession. |
| (ib) | ➤ Insurance premium paid by Federal Milk Co- Operative Society on life of cattle owned by a member of a Primary co-operative society. | ➤ Such primary society should be engaged in supplying milk raised by its members to such federal milk co-operative society. |
| (ib) | ➤ Health Insurance premium paid by any mode of payment other than cash by an employer on health of his employees under a scheme. | ➤ Such scheme must be — (a) framed by GIC and approved by Central Government, or (b) framed by any other insurer and approved by IRDA |
| (ii) | <ul style="list-style-type: none"> ➤ Bonus or commission paid to an employee for services rendered (not otherwise have been payable to him as profit or dividend). ➤ Deduction is subject to the provisions of Section 43B and Section 40A(2). | <ul style="list-style-type: none"> ➤ Voluntary payments are deductible if it is for services rendered. ➤ Any bonus exceeding the statutory amount is allowed if such excess payment has been made on account of commercial expediency |

| | | |
|----------------------|---|--|
| <p>(iii)</p> | <p>➤ Interest on capital borrowed for the purposes of business or profession.</p> <p>However, the interest paid on capital borrowed, for acquisition of an asset (whether capital used in the books of account or not); for any period beginning from the date on which the capital was borrowed for acquisition of the asset till the date on which such asset was first put to use, shall not be allowed as deduction. Thus, interest paid in respect of capital borrowed for acquisition of an asset, for the period upto the date on which the asset is first put to use to be capitalized, even if the acquisition of the asset is not for extension of existing business or profession.</p> | <p>➤ Capital means 'money'; not any other asset.</p> <p>➤ Deduction subject to Section 43B & 40(a)(i).</p> <p>➤ Interest on own capital is not deductible.</p> <p>➤ The need of assessee to borrow cannot be examined/evaluated by the Assessing Officer.</p> <p>➤ Interest on money borrowed for payment of tax or interest on late payment of advance tax or for late filing of return is not deductible.</p> <p>➤ Periodical Subscriptions paid by shareholders, or subscribers in Mutual Benefit Societies shall be deemed to be capital borrowed.</p> |
| <p>(iiia)</p> | <p>➤ Discount on zero coupon bond calculated in pro rata manner over the life of such bond.</p> <p>➤ Discount = Amount payable by issuer on maturity / redemption of such bond Less Amount received or receivable on issue of bond.</p> <p>➤ Zero coupon bond means a notified bond issued by any infrastructure capital company / fund or infrastructure debt fund or public sector company or scheduled bank, in respect of which no payment and benefit is received or receivable before maturity or redemption. (Amended by Finance Act, 2021 w.e.f. 01-04-2022 i.e. AY2022-23)</p> | <p>➤ Life of bond Period starting from the date of issue of the bond and ending on the date of maturity or redemption of such bond.</p> <p>➤ For computing life of the bond, if the month in which bond is issued or is redeemed / matured is a part of the month, then, such month shall be rounded off to the nearest one i.e. if such part is 15 days or more, it will be taken as one month, otherwise it will be ignored.</p> |
| <p>(iv)</p> | <p>➤ Contribution made by employer to recognised provident fund/approved superannuation fund</p> | <p>➤ Deduction is subject to the provisions of Section 43B.</p> |
| <p>(iva)</p> | <p>➤ Deduction of —</p> <p>(a) Contribution made by an employer towards a pension scheme, as referred to u/s 80CCD, on account of an employee; or</p> | <p>➤ 'Salary' includes dearness allowance, if the terms of employment so provide, but excludes all other allowances & perquisites.</p> |

| | | |
|--------------|--|---|
| | (b) 10% of salary of the employee in the previous year, whichever is less. | |
| (v) | ➤ Sum paid by employer towards an approved gratuity fund set up for benefit of his employees. | ➤ Deduction is subject to the provisions of Section 43B. |
| (va) | <ul style="list-style-type: none"> ➤ Sum received by assessee from his employees as contributions to Provident Fund or Employee State Insurance Fund or Superannuation fund or any other employee-welfare fund. ➤ Such sum received by the assessee is first treated as income under Section 2(24)(x) and thereafter, deduction is allowed in respect of such sum if the relevant conditions are satisfied. | <ul style="list-style-type: none"> ➤ Such sum should be credited by the assessee to the employee's account in the relevant fund(s) on or before the due date. ➤ Due date means date by which the assessee is required as an employer to credit an employee's contribution to his account in the relevant fund(s) under any law, standing order, award, contract of service or otherwise. <p>Due date not to be determined as per Section 43 [Explanation 2]: The provisions of section 43B shall not apply and shall be deemed never to have been: applied for the purposes of determining the "due date" referred hereunder. IA amended by Finance Act, 2021 w.e.f. 01-04-2021 i.e. AY 2021-221</p> |
| (vi) | ➤ Loss in respect of animals, used for business or profession (otherwise than as stock-in trade), which have died or become permanently useless. | ➤ Deduction allowed = [Actual cost of the animal — Sale proceeds of carcasses or animals] |
| (vii) | ➤ Bad debts | ➤ Discussed later. |
| (ix) | <ul style="list-style-type: none"> ➤ Expenditure incurred by a company for promoting family planning amongst its employees, ➤ Extent of deduction: <ol style="list-style-type: none"> 1) Where expenditure is of revenue nature: 100% in the previous year in which it is incurred, 2) Where expenditure is capital in nature: 1/5th of such expenditure is deductible in each of the consecutive previous years beginning with the previous year in which expenditure is incurred. | <ul style="list-style-type: none"> ➤ Any unabsorbed family planning expenditure is carried forward and set off in the same manner as unabsorbed depreciation ➤ No depreciation allowable under Section 32 if deduction has been claimed here. ➤ Tax treatment in case of sale of such asset: Same as in Section 35. |

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| (xv) | ➤ Securities Transaction Tax (STT) paid by the assessee in respect of the taxable securities transactions entered into in the course of his business during the previous year. |
| (xvi) | ➤ Commodities transaction tax (CTT) paid by the assessee in respect of the taxable commodities transactions entered into in the course of his business during the previous year, if the income arising from such taxable commodities transactions is included in the income computed under the head “Profits and gains of business or profession”. |

Deductions in relation to bad debts under section 36(1)(vii) read with 36(2):

(1) Deduction in respect of bad debts [Section 36(i)(vii) and 36(2)]: Bad debts written off as irrecoverable in the accounts (P & L A/c) of the assessee are deductible. However, no deduction is allowed for any provision for bad and doubtful debts.

Where the amount of such debt or part thereof has been taken into account in computing the income of the assessee of the previous year in which the amount of such debt or part thereof becomes irrecoverable or of an earlier previous year on the basis of income computation and disclosure standards notified under Section 145(2) without recording the same in the accounts, then, such debt or part thereof shall be allowed in the previous year in which such debt or part thereof becomes irrecoverable and it shall be deemed that such debt or part thereof has been written off as irrecoverable in the accounts for the purposes of Section 36(1)(vii)].

(2) This deduction is allowed subject to the following conditions —

(a) There must be a debt and the debt must be incidental to the business or profession of the assessee. Thus, loan advanced by a firm of solicitors to a company, in whose formation it acted as legal advisor, is not deductible on its becoming irrecoverable because that is not a part of the profession of a solicitor and such debt is not revenue in nature.

(b) Such debt must have been taken into account in computing the income of the assessee of previous year in which it is written off or of an earlier previous year; or it represents money lent in ordinary course of banking or money lending business carried on by assessee.

(3) In the case of an assessee to which Section 36(1)(vii) applies, if the amount of the actual bad-debts is greater than the provision made, then such bad-debts in excess of the provision shall be allowed as deduction under this section.

(4) In case of bad debt recovery [Section 41(4)1: In case any amount allowed as bad debt is ultimately recovered, the following sum shall be chargeable to tax whether or not the business is in existence in that previous year — Amount recovered on such debt - [Actual Amount of bad debt - Amount deducted u/s 36(1)(vii)]

If the aforesaid sum is negative, the same shall be allowed as deduction as bad debts.

(5) Successor of business — Bad debts allowable business-wise, not assessee-wise: The successor to the business is entitled to deduction in respect of the debts incurred by the predecessor if the business is not dissolved and the identity of the business after succession remains the same. Deduction for bad debts is allowed business-wise and not assessee-wise. - **CIT v. Veerbhadra Rao, K. Koteswara Rao and Co. 119851155 ITR 152 (SC)**

(6) No requirement to prove bad debts: The only requirement for availing deduction under this section is that the bad debt is written off as irrecoverable in the accounts of the assessee and there is no

necessity to establish that the debt has really become irrecoverable. - T. R. F. Ltd. v. CIT 120101323 ITR 397 (SC)

Conditions to be satisfied for the allowability of expenditure under section 37 of the Income-tax Act,

(1) General Deduction [Section 37]: The conditions to be satisfied for the allowability of expenditure u/s 37 are as follows

- i) The expenditure should not be of the nature described in Sections 30 to 36.
- ii) It should have been incurred by the assessee in the accounting year.
- iii) It should be in respect of a business carried on by the assessee the profits of which are being computed and assessed.
- iv) It must have been incurred after the business was set up.
- v) It should not be in the nature of personal expenses of the assessee.
- vi) it should not be in the nature of capital expenditure.
- vii) It should be laid out or expended wholly and exclusively for the purposes of the business or profession carried on by the assessee.

(2) Expenditure for any offence or prohibited purpose — Not allowable [Explanation I to Section 37(1)]: Any expenditure incurred by an assessee for any purpose, which is an offence, or which is prohibited by law shall not be deemed to have been incurred for the purpose of business or profession and no deduction or allowance shall he made in respect of such expenditure.

(3) CSR expenditure Not deductible [Explanation 2 to Section 37(1)]: Any expenditure incurred by an assessee on the activities relating to corporate social responsibility referred to in section 135 of the Companies Act, 2013 shall not be deemed to be an expenditure incurred by the assessee for the purposes of the business or profession.

(4) Advertisement expenditure in magazine published by political party Not deductible [Section 372B)]: No allowance shall be made in respect of expenditure incurred by an assessee on advertisement in any souvenir, brochure, tract, pamphlet or the like published by a political party.

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| <p>Circular No. 38/2016 dated 22-11-2016</p> | <p>Expenditure incurred by a firm on Keyman insurance policy of partner is admissible as deduction: Keyman insurance policy when obtained to secure the life of a partner to safeguard the firm against a disruption of the business is equally for the benefit of the partnership business which may be effected as a result of premature death of a partner. Thus, the premium on the Keyman Insurance Policy of partner of the firm is wholly and exclusively for the purpose of business and is an admissible expenditure under section 37 of the Act.</p> |
| <p>Circular No. 5/2012 dated 01-8-2012</p> | <p>Inadmissibility of expenses incurred in providing freebies to medical practitioner by pharmaceutical and allied health sector industry: The CBDT, considering the fact that the claim of any expense incurred in providing freebies to medical practitioner is in violation of the provisions of Indian Medical Council (Professional Conduct, Etiquette and Ethics) Regulations, 2002 has clarified that the expenditure so incurred shall be inadmissible under section 37(1) of the Income-tax Act, 1961,, being an expense prohibited by the law. The disallowance shall be made in the hands of such pharmaceutical or allied health sector industry or other assessee which has provided</p> |

aforesaid freebees and claimed it as a deductible expense in its accounts against income.

This circular has also clarified that a sum equivalent to value of freebees enjoyed by the aforesaid medical practitioner professional associations is also taxable as business income or income from other sources, as the case may be, depending on the facts of each case.

SPECIFIC DISALLOWANCES – SECTION 40 & 40A

Various disallowances as provided under section 40(a) while computing income under the head Profits and gains of business or profession.

| Sec.40(a) | Expenditure disallowed |
|-----------|--|
| (i) | <p>Payments outside India or to non-residents on which tax has not been deducted/paid:</p> <ul style="list-style-type: none"> ➤ Any interest, royalty, fees for technical services or other sum chargeable in the hands of recipient under this Act and payable — <ul style="list-style-type: none"> (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 such deduction, has not been paid on or before the due date of furnishing return of income specified under section 139(1). ➤ However, where in respect of any sum - <ul style="list-style-type: none"> (a) tax has been deducted in any subsequent year; or (b) has been deducted during the P.Y. but paid after the due date specified in section 139(1), then, such sum shall be allowed as a deduction in computing the income of the subsequent previous year in which the TDS has been so paid. ➤ Where an assessee fails to deduct the whole or any part of the tax in accordance with the provisions of Chapter XVII-B on any such sum but is not deemed to be an assessee in default under the first proviso to Section 200(1), by reason that such payee — <ul style="list-style-type: none"> (a) has furnished his return of income under section 139; (b) has taken into account such sum for computing income in such return of income; and (c) has paid the tax due on the income declared by him in such return of income, and the payer furnishes a certificate to this effect from an accountant in such form as may be prescribed, <p>it would be deemed that the assessee has deducted and paid the tax on such sum on the date on which return of income has been furnished by the payee.</p> <p>Since the date of furnishing the return of income by the payee is taken to be the date on which the payer has deducted tax at source and paid the same, such expenditure/payment in respect of which the payer has failed to deduct tax at source shall be disallowed under section 40(a)(i) in the year in which 11w said expenditure is incurred, However, such expenditure will be allowed as deduction in the subsequent</p> |

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| | <p>year in which the return of income is furnished by the payee, since tax is deemed to have been deducted and paid by the payer in that year.</p> <p>For example: If TDS on interest payable outside India during financial year 2021-22 is not paid in 2021-22, but is paid on or before 31-10-2022 (being due date of furnishing return of Income), such interest shall be allowed as deduction in assessment year 2022-23 (i.e. previous year 2021-22) only. However, if such TDS is paid on 01-11-2022 i.e. after the expiry of the due date of filing return of income, then the deduction for such payment shall be allowed during assessment year 2023-24 (previous year 2022-23).</p> |
| (ia) | <p>Payments to residents on which tax has not been deducted/ paid — 30% of such sum shall not be allowed as deduction:</p> <ul style="list-style-type: none"> ➤ 30% of any sum payable to a resident on which — <ul style="list-style-type: none"> (a) tax is deductible at source and such tax has not been deducted; or (b) after such deduction, has not been paid on or before the due date of furnishing return of income specified under section 139(1). ➤ However, where in respect of any sum - <ul style="list-style-type: none"> (a) tax has been deducted in any subsequent year; or (b) has been deducted during the previous year but paid after the due date specified in Sec. 139(1), then, 30% of such sum shall be allowed as a deduction in computing the income of the subsequent previous year in which the TDS has been so paid. ➤ Where an assessee fails to deduct the whole or any part of the tax on any such sum but is not deemed to be an assessee in default under the first proviso to Section 201(1) (i.e. payee has deposited self-assessment tax directly), then, it shall be deemed that the assessee has deducted and paid the tax on such sum on the date of furnishing of return of income by the payee. <p>For example: The tax amounting to Rs.10,000 was deductible in previous year 2021-22 in respect of interest of Rs.1 lakh payable to a resident. Such interest of Rs.1,00,000 will be allowed as deduction during the previous year,2021-22 only if the tax of Rs.10,000 is deducted in 2021-22 and is paid on or before due date specified under section 139(1) However, if such tax is deducted in 2021-22 and is paid in 2022-23 ,after due date specified u/s 139(1), then, 30% of such interest (i.e. 30,000) will not be allowed as deduction in the previous year 2021-22 but the same will be allowed as deduction in previous year 2022-23. Further, if the tax relating to such interest payment is deducted on or after 14-2022, then, 30% of such interest shall not be allowed only in the year 2021-22, even if the same is paid on or before due date specified in section 139(1) for furnishing return of Income for assessment year 2022-23.</p> |
| (ii) | <p>Income-tax: Any sum paid on account of any rate or tax levied on the profits or gains of any business or profession or assessed at a proportion of, or otherwise on the basis of, any such profits or gains (i.e. income-tax).</p> <p>Any income tax paid outside India and eligible for relief of tax under section 90 or 90A or 91 shall also not be deductible.</p> |
| (iia) | <p>Wealth-tax: Any sum paid on account of wealth-tax.</p> |

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| (iib) | <p>Certain fees, Royalty, Service charges etc. payable by State Government undertaking to the State Government:</p> <p>Any amount—</p> <p>(A) 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</p> <p>(B) which is appropriated, directly or indirectly, from, a State Government undertaking by the State Government.</p> |
| (iii) | <p>Payment of Salaries outside India or to non-residents on which tax has not been deducted and paid:</p> <p>Any payment which is chargeable under the head “Salaries”, if it is payable —</p> <p>(a) outside India; or</p> <p>(b) to a non-resident,</p> <p>and if the tax has not been paid thereon nor deducted therefrom under Chapter XVII-B.</p> <p>[Note: Even if tax is deducted on such salary in subsequent previous year, such salary shall not be allowed as deduction in that previous year.]</p> |
| (iv) | <p>Contribution towards Employees welfare fund: Any payment by the employer to provident fund or other fund established for the benefit of the employees of the assessee, unless he has made effective arrangements to secure that tax shall be deducted at source from any payments made from the fund which are taxable under the head “Salaries”.</p> |
| (v) | <p>Tax paid by employer on non-monetary perquisites: Any tax actually paid by an employer on non- monetary perquisites, as referred to in Section 10(10CC).</p> |

Question 18: Section 40(a)(i): X Ltd. pays a sum of Rs.10,00,000 as commission to Y Inc. (a US company) on October 15, 2022. Tax is deductible under section 195 (read with Indo-US tax treaty) but it is not deducted by X Ltd. Y Inc. pays advance tax on the due dates on its income (including Rs.10,00,000). Entire tax liability is paid by Y Inc. during the financial year 2022-23 by way of advance tax. Return of income of Y Inc. for the assessment year 2023-24 is submitted on September 20, 2023. X Ltd. has a certificate of this effect from a chartered accountant in the prescribed form. Discuss tax consequences in respect of the said transaction in hands of X Ltd.

Solution: In this case, X Ltd. has not deducted tax at source in the financial year 2022-23. By virtue of section 40(a)(i), the payment of Rs.10,00,000 will be disallowed in computing the income for the assessment year 2023-24. However, X Ltd. cannot be treated as an assessee-in-default under the amended provisions of first proviso to section 201(1), as the following conditions are satisfied---

- (a)** Y Inc. has furnished its return of income under section 139;
- (b)** Y Inc. has taken into account the above income in such return of income;
- (c)** Y Inc. has paid the tax due on the income declared in such return of income, and
- (d)** X Ltd. has a certificate to this effect from a chartered accountant in a prescribed form.

Under the amended provisions, it will be assumed that X Ltd. has deducted and paid tax on September 20, 2023, As a consequence, Rs.10,00,000 will be allowed as deduction in the hands of X Ltd. for the financial year 2022-23 (i.e. assessment year 2023-24).

Question 19: Deductibility of various expenses: State with reasons, the allowability of the following expenses incurred by MN Limited, a wholesale dealer of commodities, under the Income-tax Act, 1961 while computing Profit & Gains from business or profession for the Assessment Year 2023-24.

- (a) Construction of school building in compliance with CSR activities amounting to Rs.5,60,000.
- (b) Purchase of building for setting up a warehousing facility for storage of food grains amounting to Rs.4,50,000.
- (c) Interest on loan paid to Mr. X (a resident) Rs.50,000 on which tax has not been deducted.
- (d) Commodity transaction tax paid Rs.20,000 on sale of bullion. **(8 Marks, Nov. 2015)**

Ans:

- (a) According to Explanation 2 to Section 37(1), Any expenditure incurred by an assessee on the activities relating to corporate social responsibility referred to in section 135 of the Companies Act, 2013 shall not be deemed to be an expenditure incurred by the assessee for the purposes of the business or profession. Hence, expenditure incurred on construction of school building in compliance with SR activities amounting to Rs.5,60,000 will not be allowed as deduction.
- (b) 100% of the expenditure incurred on purchase of building for setting up a warehousing facility for storage of food grains is eligible for deduction under Section 35AD. Hence, the company will be eligible for deduction of 100% of Rs.4,50,000 in accordance with the provisions of Section 35AD.
- (c) According to Section 40(a)(ia) - 30% of any sum payable to a resident on which tax is deductible at source and such tax has not been deducted; or after such deduction, has not been paid on or before the due date of furnishing return of income specified under section 139(1) shall not be allowed as deduction. Hence, 30% of Rs.50,000 = Rs.15,000 shall not be allowed as deduction while computing Profits and Gains of Business or Profession.
- (d) According to Section 36(1)(xvi), Commodities transaction tax paid by the assessee in respect of the taxable commodities transactions entered into in the course of his business during the previous year, if the income arising from such taxable commodities transactions is included in the income computed under the head "Profits and gains of business or profession" shall be allowed as deduction. Hence, commodity transaction Tax paid Rs.20,000 on sale of bullion shall be admissible as deduction.

Provisions relating to computation of Profits and Gains of Business or Profession of Firm:

In computing the income under the head Profits and Gains of Business or Profession of a firm which is assessed as such, the following amounts shall be disallowed in accordance with the provisions of Section 40(b),—

- (i) any payment of salary, bonus, commission or remuneration, to any partner who is not a working partner, i.e. non-working partner; or
- (ii) any payment of remuneration to any partner who is a working partner, or of interest to any partner, which, is not authorised by, or which is not in accordance with, the terms of the partnership deed; or
- (iii) any payment of remuneration to any partner who is a working partner. or of interest to any partner, which, is authorised by and is in accordance with, the terms of the partnership deed, but which relates to any period prior to the date of such partnership deed unless authorised by earlier partnership deed; or

(iv) any interest paid to any partner in excess of 12% simple interest p.a.;

(v) **Remuneration to working partners:** Remuneration paid to working partners during the previous year shall not be allowed to the extent it exceeds, in aggregate, the following limits —

| Book profits | Allowable Remuneration |
|--|---|
| On first Rs.3,00,000 of book profits, or, in case of a loss. | ➤ Rs.1,50,000, or ➤ 90% of book profits, whichever is more. |
| On balance of the book profits | 60% of the book profits. |

➤ **Explanation 1:** Where an individual is a partner in a firm on behalf, or for the benefit, of any other person (such partner and the other person being hereinafter referred to as “partner in a representative capacity” and “person so represented”, respectively),—

(a) interest paid by the firm to such individual, otherwise than as partner in a representative capacity, shall not be taken into account for the purposes of this section;

(b) interest paid by the firm to such individual as partner in a representative capacity and interest paid by the firm to the person so represented shall be taken into account for the purposes of this section.

For example: Mr. X (HUF) is a partner in XYZ firm, where Mr. X is representing his HUF. If personal funds of Mr. X are invested in the firm, then such interest shall not be disallowed even, if it exceeds. 12% p.a. However, interest paid to X for HUF or to the HUF shall be disallowed in excess of 12% p.a

➤ **Explanation 2:** Where an individual is a partner in a firm otherwise than as a partner in a representative capacity, interest paid by the firm to such individual shall not be taken into account for the purposes of this section, if such interest is received by him on behalf, or for the benefit, of any other person.

For example: Mr. X is a partner in a firm in his personal capacity. His minor son has invested funds in the firm. In this case, interest paid to Mr. X for funds of his minor son shall not be disallowed under section 40(b).

➤ **Explanation 3: “Book-profit”** means the net profit, as shown in the P&L A/c 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.

➤ **Explanation 4 “Working partner”** means an individual who is actively engaged in conducting the affairs of the business or profession of the firm of which he is a ‘partner’.

OTHER PROVISIONS:

(1) **Exemption to partners in respect of their share in firm’s income [Section 10(2A):** In 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 shall not be included in his total income.

$$\text{Share of partner in the total income of firm} = \frac{\text{Total income of the firm} \times \text{amount of partner's share in the profit of the firm in accordance with the partnership deed}}{\text{Total profit of the firm}}$$

Circular No. 8 dated
3V March, 2014

Clarification of interpretation of provision of section 10(2A) of the Income-tax Act, 1961 in regard to cases where laconic of the firm is exempt.

➤ It is clarified that 'total income' of the firm for section 10(2A) of the Act, includes income which is exempt or deductible under various provisions of the Act.

Income of a firm is to be taxed in the hands of the firm only and the same can under no circumstances be taxed in the hands of its partners.

➤ Therefore, it is further clarified that the entire profit credited to the partners' accounts in the firm would be exempt from tax in the hands of such partners, even if the income chargeable to tax becomes NIL in the hands of the firm on account of any exemption or deduction as per the provisions of the Act.

(2) Interest, salary, etc. received by a partner to be assessed as his business income [Section 28(v)]:

Any interest, salary, bonus, commission or remuneration due to or received by a partner from a firm shall be chargeable to income-tax under the head Profits and Gains of Business or profession. However, where such payment has not been allowed to be deducted under Section 40(b) in the hands of the firm, then it shall be exempt in the hands of the partner.

Question 20: Computation of book profit and allowable remuneration: Rao & Jain, a partnership firm consisting of two partners, reports a net profit of Rs.7,00,000 before deduction of the following items,

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

Compute:

- (i) Book-profit of the firm under section 40(b) of the Income-tax Act, 1961.
- (ii) Allowable working partner salary as per section 40(k) of the Income-tax Act, 1961,.

Solution: Computation of book profits and allowable working partner salary (amounts in Rs.)

| | | |
|--|----------|-----------------|
| Net profit as per Profit & Loss account | | 7,00,000 |
| Less: (a) Depreciation u/s 32 | 1,50,000 | |
| (b) Interest on capital to the extent of 12% p.a. on Rs.5,00,000 | | 2,10,000 |
| Book Profits | | 4,90,000 |

Computation of allowable of remuneration amount in Rs.):

| | | |
|---|----------|----------|
| Actual Remuneration (Rs.20,000 p.m. x 12 months x 2 partners) | | 4,80,000 |
| Remuneration allowable u/s 40(b) | | |
| On the first Rs.3,00,000 of book profit [(Rs.1,50,000 or 90% of Rs.3,00,000) whichever is more] | 2,70,000 | |
| On the balance of book profit[60% of (Rs.4,90,000 – Rs.3,00,000)] | 1,14,000 | 3,84,000 |

| | | |
|---|--|----------|
| Maximum allowable remuneration (lower of actual remuneration or remuneration as per section 40(10)) | | 3,84,000 |
|---|--|----------|

Question 21: Remuneration allowable u/s 40(b): Nikhil, Gagan and Sdrn4n are partners in a equal shares. The profit and loss account for the year ending 31st March, 2023 shows a net profit of Rs.42,300 after debiting the following items:

(i) Salary of Rs.74000 each to Nikhil and Gagan

(ii) Bonus to Suman Rs.68,000

(iii) Commission of Rs.19,000, Rs.20,000 and Rs.45,000 to Nikhil, Gagan and Suman respectively.

(iv) Interest on capital @ 15% amounting to Rs.4,500, Rs.6,000 and Rs.15,000 was paid to Nikhil, Gagan and Suman respectively.

Assuming that all partners are working partners and the firm fulfils the conditions of Section 184, compute the total income of the firm and taxable income of the partners in the firm;

Solution: Calculation of total income of the firm (amount in Rs.):

| | | |
|--|----------|-----------------|
| Net profit as per Profit and Loss A/c | | 42,300 |
| Add: Disallowed items: | | |
| Salary to Partners (Nikhil Rs.74,000 + Gagan Rs.74,000) | 1,48,000 | |
| Bonus to Suman | 68,000 | |
| Commission to Partners (Nikhil Rs.19,000 + Gagan Rs.20,000 + Suman Rs.45,000) | 84,000 | 3,00,000 |
| Interest to partners in excess of 12% p.a. — | | |
| Nikhil = (Rs.4,500 x 3) ÷ 15 | 900 | |
| Gagan = (Rs.6,000 x 3) ÷ 15 | 1,200 | |
| Suman = (Rs.15,000 x 3) ÷ 5 | 3,000 | 5,100 |
| Book profits | | 3,47,400 |
| Less: Allowable remuneration allowable under section 40(b), being lower of the following — | | |
| (a) Actual remuneration; or | 3,00,000 | |
| (b) Allowable u/s 10(b) [Rs.3,00,000 x 90% + Rs.47,400 x 60%] | 2,98,440 | 2,98,440 |
| Total income | | 48,960 |

Calculation of total income of each partner of the firm (amount in Rs.):

| Particulars | Nikhil | Gagan | Suman |
|---|---------------|---------------|-----------------|
| Interest on capital @ 12% (to the extent allowed in hands of the firm) | 3,600 | 4,800 | 12,000 |
| Salary, Bonus & Commission (taxable only upto Rs.2,98,440 since the same is allowed in hands of firm) | 92,516 | 93,511 | 1,12,412 |
| Total income | 96,116 | 98,311 | 1,24,412 |

Provisions for computing business income of any AOP/BOI [Section 40(ba)]:

In computing I-he income of an AOP/BOI under the head, 'Profits and gains of business or profession', the following shall be disallowed —

(1) **Interest to members - Not allowable:** Any payment of interest, made by such association or body to a member of such association or body.

Note:

- (a) Where interest is paid by an association or body to any member thereof who has also paid interest to the association or body, then net amount of interest shall be disallowed.
- (b) Where an individual is a member of an association or body on behalf, or for the benefit, of any other person (such member and the other person hereinafter referred to as “member in a representative capacity” and “person so represented”, respectively),
 - (i) interest paid by the association or body to such individual or by such individual to the association or body otherwise than as member in a representative capacity, shall not be disallowed.
 - (ii) interest paid by the association or body to such individual or by such individual to the association or body as member in a representative capacity and interest paid by the association or body to the person so represented or by the person so represented to the association or body, shall be disallowed.
- (c) Where an individual is a member of an association or body otherwise than as member in a representative capacity, interest paid by the association or body to such individual shall not be disallowed, if such interest is received by him on behalf, or for the benefit, of any other person.

(2) Remuneration to members - Not allowable: Any payment of salary, bonus, commission or remuneration, by whatever name called, made by such association or body to a member of such association or body.

Question 22: Computation of total income of AOP: M/s. XYZ, an association of person, consisting of members X, Y & Z sharing profits in the ratio of 2 : 2 : 1, furnishes you with the following information:

Net profit as per P & L A/c is Rs.6 lakhs after following debits:

Salaries paid to members: Mr. X Rs.1,60,000, Mr. Y Rs.2,40,000 and Mr. Z Rs.1,20,000.

Interest on capital to members @ 15% p.a.: Mr. X Rs.45,000, Mr. Y Rs.60,000 and Mr. Z Rs.15,000.

Determine the income of association of person.

Solution: Computation of total income of AOP (amounts in Rs.):

| | | |
|---|----------|------------------|
| Net profit as per Profit and Loss Account | 6,00,000 | |
| Add: Salaries to members | | |
| Mr. X | 1,60,000 | |
| Mr. Y | 2,40,000 | |
| Mr. Z | 1,20,000 | 5,20,000 |
| Add: Interest on capital | | |
| Mr. X | 45,000 | |
| Mr. Y | 60,000 | |
| Mr. Z | 15,000 | 1,20,000 |
| Total income of the AOP | | 12,40,000 |

Disallowance of Payment made to specified persons/relatives in excess of fair market value [Section 40A(2)]:

(1) Payment to relatives in excess of fair value — Not deductible: If the —

- (a) assessee incurs any expenditure in respect of which payment has been or is to be made to ‘specified persons’; and

(b) the Assessing Officer is of opinion that such expenditure is excessive or unreasonable having regard to—

(i) the fair market value of goods, services or facilities for which the payment is made; or

(ii) the legitimate needs of the business or profession of the assessee; or

(iii) the benefit derived by or accruing to assessee therefrom;

then, so much of the expenditure as is so considered by the Assessing Officer to be excessive or unreasonable shall not be all owed as deduction.

Thus, amount to be disallowed Expenditure incurred - FMV of goods/services/facilities/benefit etc. received by the assessee.

(2) Meaning of Specified persons: The Specified Persons are the following, namely -

| | | |
|--------------|--|--|
| (i) | Where the assessee is an individual | Any relative of the assessee; |
| (ii) | Where the assessee is a company, firm, association of persons or Hindu undivided family | Any director of the company, partner of the firm, or member of the association or family, or any relative of such director, partner or member; |
| (iii) | Any individual who has a substantial interest in the business or profession of the assessee, or any relative of such individual; | |
| (iv) | A company, firm, association of persons or Hindu undivided family having a substantial interest in the business or profession of the assessee or any director, partner or member of such company, firm, association or family, or any relative of such director, partner or member, or any other company carrying on business or profession in which the first mentioned company has substantial interest; | |
| (v) | A company, firm, association of persons or Hindu undivided family of which a director, partner or member, as the case may be, has a substantial interest in the business or profession of the assessee; or any director, partner or member of such company, firm, association or family or any relative of such director, partner or member | |
| (vi) | Any person who carries on a business or profession,— (A) where the assessee being an individual, or any relative of such assessee, has a substantial interest in the business or profession of that person; or (B) where the assessee being a company, firm, association of persons or Hindu undivided family, or any director of such company, partner of such firm or member of the association or family, or any relative of such director, partner or member, has a substantial interest in the business or profession of that person. | |

Substantial Interest' and two situations in which the same assumes importance

As per Explanation to Section 40A(2), a person shall be deemed to have a substantial interest in a business or profession, if —

(a) in a case where the business or profession is carried on by a company, such person, at any time during the previous year, is the beneficial owner of equity shares carrying not less than 20% of the voting power; and

(b) in any other case, such person, at any time during the previous year, is beneficially entitled to not less than 20% of the profits of such business or profession.

The situations where the substantial interest assumes importance are,

- (i)** Taxability of deemed dividend under section 2(22)(e);
- (ii)** Disallowance of excessive or unreasonable expenditure under section 40A(2) to an individual who has substantial interest in the business or profession of the assessee;
- (iii)** Clubbing of salary income of spouse under section 64(1)(ii) in respect of remuneration received by the spouse from a concern in which the individual has a substantial interest.

Disallowance in respect - of payment of an expenditure in excess of Rs.10,000 otherwise than by an account payee cheque drawn on a bank or account payee bank draft while computing Profits and gains of business of profession.

(1) Expenditure paid in aggregate exceeding Rs.10,000 in a day, otherwise than by account payee cheque or account payee bank draft [Section 40A(3)] Where the assessee incurs any expenditure in respect of which a payment or aggregate of payments made to a person in a day, otherwise than by an account payee cheque drawn on a bank or account payee bank draft or use of electronic clearing system through a bank account or through such other electronic mode as may be prescribed, exceeds Rs.10,000, no deduction shall be allowed in respect of such expenditure. [(a) Credit Card; (b) Debit Card; (c) Net Banking; (d) IMPS (Immediate Payment Service,); (e) UPI (Unified Payment Interface (f) RTGS (Real Time Gross Settlement); (g) NEFT (National Electronic Funds Transfer,), and (h) BHIM (Bharat Interface for Money) Aadhar Pay have been prescribed as mode of electronic payment)

(2) Disallowance to be made in the year of payment for expenditure incurred in earlier years [Section 40A(3A)]: Where -

- (a)** an allowance has been made in the assessment for any year in respect of any liability incurred by the assessee for any expenditure; and
- (b)** subsequently, during any subsequent year, the assessee makes payment in respect thereof, otherwise than by an account payee cheque drawn on a bank or account payee bank draft or use of electronic clearing system through a bank account or through such other electronic mode as may be prescribed, and
- (c)** the payment or aggregate of payments so made to a person in a day exceeds Rs.10,000; then, the payment so made shall be deemed to be the profits and gains of business or profession and accordingly chargeable to income-tax as income of the subsequent year. 1(a) Credit Card; (b) Debit Card; (c) Net Banking; (d) IMPS (Immediate Payment Service,); (e) UPJ (Unified Payment Interface); (ft RTGS (Real Time Gross Settlement); (g,) NEFT (National Electronic Funds Transfer,), and (li) BHIM (Bharat Interface for Money) Aadhar Pay have been prescribed as mode of electronic payment)

(3) No disallowance shall be made and no payment shall be deemed to be the profits and gains of business or profession, in such cases and under such circumstances as may be prescribed, having regard to the nature and extent of banking facilities available, considerations of business expediency and other relevant factors.

(4) Enhanced limit of Rs.35,000 in case of goods transport agencies: In the case of payment made for plying, hiring or leasing goods carriages, the aforesaid limit shall be Rs.35,000 instead of Rs.10,000.

(5) No person to enforce that payment exceeding Rs.10,000/ Rs.35,000 to be made in cash [Section 40A(4)]: Where any payment in respect of any expenditure has to be made by an account payee cheque drawn on a bank or account payee bank draft or use of electronic clearing system through a bank account or through such other electronic mode as may be prescribed in order that such expenditure may not be disallowed as a deduction under this section, then the payment may be made by such cheque or draft or electronic clearing system or through such other electronic mode as may be prescribed and where the payment is so made or tendered, no person shall be allowed to raise, in any suit or other proceeding, a plea based on the ground that the payment was not made or tendered in cash or in any other manner. [(a) Credit Card; (b) Debit Card; (c) Net Banking; (d) IMPS (Immediate Payment Service); (e) UPI (Unified Payment Interface); (f) RTGS (Real Time Gross Settlement); (g) NEFT (National Electronic Funds Transfer), and (h) BHIM (Bharat Interface for Money) Aadhar Pay have been prescribed as mode of electronic payment.

(6) Cases where disallowances would not be attracted:

(i) Loan transactions: It does not apply to loan transactions because advancing of loans or repayments of the principal amount of loan does not constitute an expenditure deductible in computing the taxable income. However, interest payments of amounts exceeding 10,000 at a time are required to be made by account payee cheques or drafts or electronic clearing system or through such other prescribed electronic modes as interest is a deductible expenditure.

(ii) Payment made by commission agents: This requirement does not apply to payment made by commission agents for goods received by them for sale on commission or consignment basis because such a payment is not an expenditure deductible in computing the taxable income of the commission agent.

For the same reason, this requirement does not apply to advance payment made by the commission agent to the party concerned against supply of goods.

However, where commission agent purchases goods on his own account but not on commission basis, the requirement will apply. The provisions regarding payments by account payee cheque or draft or electronic clearing system or through such other prescribed electronic modes apply equally to payments made for goods purchased on credit.

The circumstances where the provisions of Section 40A(3) regarding cash payments in excess of Rs.10000 does not apply.

Provisions of Section 40A(3) not to apply in certain cases: The exceptions to Section 40A(3) are given in Rule 6DD, which are as follows —

1. Where the payment is made to RBI, any banking company, State Bank of India or its subsidiary banks, any cooperative bank or land mortgage bank, any primary agricultural credit society or any primary credit society or the Life insurance Corporation of India;
2. Where the payment is made to the Government and under the rules framed by it, such payment is required to be made in legal tender;
3. Where the payment is made through any bank, including foreign bank, by any of these modes -
 - i) any letter of credit arrangements;

- ii) a mail or telegraphic transfer;
 - iii) a book adjustment between banks;
 - iv) a bill of exchange made payable only to a bank;
 - v) Electronic clearing system;
 - vi) a credit card;
 - vii) a debit card;
4. Where payment is made by way of adjustment against the amount of any liability incurred by the payee for any goods supplied or services rendered by the assessee to such payee;
 5. Where payment is made to the cultivator, grower or producer of the following for purchase thereof
 - (a) agricultural or forest produce; or
 - (b) produce of animal husbandry (including livestock, meat, hides and skins) or dairy or poultry farming;
 - (c) fish or fish products;
 - (d) the products of horticulture or apiculture;
 6. Where the payment is made for the purchase of the products manufactured or processed without the aid of power in a cottage industry, to the producer of such products;
 7. Where the payment is made in a village or town, which on the date of such payment is not served by any bank, to any person who ordinarily resides, or is carrying on any business, profession or vocation, in any such village or town;
 8. Where any payment is made to an employee of assessee or the heir of any such employee, on or in connection with the retirement, retrenchment, resignation, discharge or death of such employee, on account of gratuity, retrenchment compensation or similar terminal benefit and the aggregate of such sums payable to employee or his heir does not exceed Rs.50,000;
 9. Where the payment is made by an assessee by way of salary to his employee after deducting the income-tax at source, when such employee is temporarily posted for a continuous period of 15 days or more in a place other than his normal place of duty or on a ship, and does not maintain any account in any bank at such place or ship;
 10. Where the payment is made by any person to his agent who is required to make payment in cash for goods or services on behalf of such person;
 11. Where the payment is made by an authorised dealer or a money changer against purchase of foreign currency or travellers cheques in the normal course of his business.

No disallowance in case of calculation of profit at net profit rate: Where the Assessing Officer has applied net profit rate in computing the business income, no disallowance can be made under section 40A(3) because no deduction of any expenditure was allowed in computing such income.

Deduction is allowed for provision made in respect of gratuity?

1. **Provision made for unapproved gratuity fund - Not allowable:** No deduction shall be allowed in respect of any provision made by the assessee for the payment of gratuity to M/s employees on their retirement or on termination of their employment for any reason.

However, any provision made by the assessee for the purpose of contribution towards an approved gratuity fund, or for the purpose of payment of any gratuity, that has become payable during the previous year, shall be allowed as deduction.

- 2. Payment of gratuity to retiring employee — Allowable:** Where any provision, made by the assessee for the payment of gratuity to his employees on their retirement or termination of their employment has been allowed as a deduction in computing the income of the assessee for any assessment year, then any sum paid out of such provision by way of contribution towards an approved gratuity fund or by way of gratuity to any employee, shall not be allowed as a deduction in computing the income of the assessee of the P.Y. in which the sum is so paid.

Note: The deduction allowed shall be subject to the provisions of Section 43B

Deductibility of payments made to Non-Statutory Funds.

Payment made to Non-Statutory Funds - Not deductible [Section 40A(9)]: No deduction shall be allowed in respect of any sum paid by an employer towards the setting up or formation of, or as contribution to, any fund, trust, company, association of persons, body of individual's, registered society, or other Institutions for any purpose.

However, deduction shall be allowed in case such sum is paid as per provisions under section 36(1)(iv)/(iva/ (v) or under any other law for time being in force.

Question 23: Payments to relatives us 40A(2) and Cash payments u/s 40A(3): M/s XYZ, a firm constituting partners X, Y and Z, is engaged in wholesale business of electronics and made following payments towards some purchases on 01-12-2022

| Party | Mode of payment | Amount (Rs.) | Fair value (Rs.) |
|-----------------------------------|----------------------|--------------|------------------|
| Raj Ltd | Cash | 89,000 | 10,000 |
| PQR and Co | Account payee cheque | 65,000 | 65,000 |
| Mr. Bansal (Bill No 100) | Crossed cheque | 15,000 | 8,000 |
| Mr. Bansal (Bill No. 101) | Cash | 5000% | 8,000 |
| Freight paid to Shiv Transporters | Cash | 30,000 | 30,000 |

X holds 25% equity shares of Raj Ltd. Y's son Ram is 60% partner in PQR and Co. Mr. Bansal is father of Z. What amount will be disallowed as per Income – tax Act, 1961?

Solution: Here, X and Y have substantial interest in Raj Ltd. and PQR and Co. respectively; and Mr. Bansal is a relative of Z. Thus, all the three patties are specified persons as per Section 40A(2). So, firstly, disallowance will be made as per Section 40A(2); and Section 40A(3) will apply to amount available after disallowance under section 40A(2).

The amount of disallowance will be computed as follows (amounts in Rs.)

| Purchases from | Disallowance u/s 40A(2) [Expenditure — Fair Value] | Disallowance u/s 40A(3) for cash payment exceeding Rs.10,000 |
|----------------|---|---|
| Raj Ltd. | Rs.70,000 [Rs.80,000 — Rs.10,000] | Nil, [WN-1] |
| PQR and Co. | Nil | NIL [Since payment is made through account payee cheque] |

| | | | |
|-------------------|--|------------------|----------|
| Mr. Bansal | Rs.7,000 [Rs.15,000 - Rs.8,000, for 1 st purchase] Nil [for 2 nd purchase, as FMV is higher] Nil | Rs.13,000 | [WN-2] |
| Shiv Transporters | | Nil | [WN - 3] |
| Total | Rs.77,000 | Rs.13,000 | |

Working Notes:

- (1) Since after disallowance under section 40A(2) of Rs.70,000, remaining allowable expenditure is Rs.10,000 since, the amount does not exceed Rs.10,000 i.e. within the prescribed limit of Section 40A(3), disallowance under section 40A(3) is not attracted.
- (2) While individual bills do not exceed Rs.10,000, but since cash payment made to Mr. Bansal on the day exceeds Rs.10,000, hence, it will be disallowed.
- (3) Payment to goods transport agency in cash shall be allowed as deduction since maximum limit for cash payment in such case is Rs.35,000.

Question 24: Allowable expenditure: Discuss the tax implications of the following in the case of a doctor running a nursing home (amount in Rs.) (CA May 2001)

| Cases | Deduction |
|--|-----------|
| (1) Amount paid to a scientific research association approved by the Central Government and run by a drug manufacturing company | 20,000 |
| (2) Payments made in cash towards purchases of medicines | 50,000 |
| (3) Amounts received from the employees of the nursing home as contributions towards Provident Fund for the month of March 2023, paid to the P.F. Commissioner on 25-4-2023. | 25,000 |

Solution: Tax implications of the following in the case of a doctor running a nursing home (amounts in Rs.)

| Cases | Deduction |
|---|-----------------|
| (1) Amount paid to a scientific research association approved by the Central Government and run by a drug manufacturing company | [WN - 1] 20,000 |
| (2) Payments made in cash towards purchases of medicines | [WN - 2] Nil |
| (3) Amounts received from the employees of the nursing home as contributions towards Provident Fund | [WN - 2] Nil |

Working Notes:

- (1) 100% of such expenditure is allowable as deduction under section 35(1)(ii) i.e. 100% of Rs.20,000 = Rs.20,000.
- (2) Such cash payments are not allowable under section 40A(3) since the same exceeds Rs.10,000.
- (3) The amount received will be first included in income of the assessee and then deduction shall be allowed under section 36(1)(va) if payment is made on or before due date of relevant fund i.e. 15.04-2023. + 15 days. in this case since payment was made on 25-04-2023 therefore no deduction shall be allowed under section 36(1)(va).

DEEMED PROFITS – SECTION 41

Deemed Profits chargeable to tax under Section 41. (Nov. 2000, May 2001)

Ans: Profits chargeable to tax [Section 41]: The deemed profits chargeable to tax under section 41 are

| Section | Deemed Profits |
|--------------|--|
| 41(1) | <p>Recovery against a deduction allowed in any previous year: Where an allowance or deduction has been made in the assessment for any year in respect of loss, expenditure or trading liability incurred by the assessee and subsequently during any previous year</p> <p>(i) the assessee has obtained, whether in cash or in any other manner whatsoever;</p> <p>(ii) any amount in receipt of such loss or expenditure or some benefit in respect of such trading liability by way of its remission or cessation thereof;</p> <p>then, the amount obtained by such person or the value of benefit accruing to him shall be deemed to be profits and gains of business or profession and accordingly, taxable as the income of that previous year,</p> <p>Whether the business or profession is in existence in that year or not.</p> <p>The same provisions shall apply in case of succession of business, in which the amount received shall be taxable in the hands of the successor.</p> <p>Unilateral Act covered [Explanation 1]: The expression “loss or expenditure or some benefit in respect of any such trading liability by way of remission or cessation thereof” shall include the remission or cessation of any liability by a unilateral act by the assessee or successor by way of writing off such liability in his accounts.</p> <p>Successor in Business [Explanation 2]: “Successor in business” means —</p> <p>(a) In case of amalgamation or demerger, the amalgamated or resulting company; and</p> <p>(b) In case assessee/firm carrying on business or profession is succeeded by any other person/firm in that business or profession, the other person / firm.</p> <p>Note: The amount so obtained shall be taxable only when it is actually received, even if the assessee follows accrual system of accounting.</p> |
| 41(4) | Taxability of Balancing Charge in case of Power Generating Undertakings. (Already discussed) |
| 41(3) | Sale of an asset used for scientific research without having been used for the purposes of business or profession. (Already discussed) |
| 41(4) | Recovery of bad debts. (Already discussed) |
| 41(5) | <p>Set off of loss against incomes taxable under section 41(1) / 41(3) / 41(4)</p> <p>Where —</p> <ul style="list-style-type: none">➤ the business or profession is no longer in existence; and➤ there is income chargeable to tax under section 41(1) or 41(3) or 41(4) in respect of that business or profession;➤ any loss, not being a loss sustained in speculation business, which arose in that business or profession during the previous year in which it ceased to exist and which could not be set off against any other income of that previous year;➤ shall be set off against such deemed profits to the extent of such profits. |

Expenses which otherwise are deductible shall be disallowed, unless payments are actually made within the due date for furnishing the return of income under Section 19(1) When can the deduction be claimed, if paid after the said date.

Certain deductions to be allowed only on actual payment [Section 43B] Notwithstanding anything contained in any other provision of the Act, a deduction of the following sums paid by the assessee, otherwise allowable under this Act, shall be allowed (irrespective of the previous year in which the liability to pay such sum was incurred according to the method of accounting regularly employed) in that previous year in which such sum is actually paid by him,-

- (i) Any sum payable by the assessee by way of tax, duty, cess or fee, by whatever name called, under any law for the time being in force; or
- (ii) Any sum payable by the assessee as an employer by way of contribution to any provident fund or superannuation fund or gratuity fund or any other fund for the welfare of employees; or
- (iii) Any bonus or commission to employees for services rendered as referred under section 36(1) Qi); or
- (iv) Any sum payable by the assessee as interest on any loan or borrowing from -
 - (i) Any Public Financial Institution (e.g. ICICI, IFCI, IDBI, LIC, UTI etc.); or
 - (ii) State Financial Corporation, or State Industrial Investment Corporation, in accordance with the terms and conditions of the agreement governing such loan or borrowing; or;
- (v) Any sum payable by the assessee as interest on any loan or borrowing from a deposit taking non-banking financial company or systemically important non-deposit taking non-banking financial company, in accordance with the terms and conditions of the agreement governing such loan or borrowing, or

Explanation

(i) Non-banking financial company means —

- a financial institution 'which is a company,
- a non-banking institution which is a company and which has as its principal business the receiving of deposits, under any scheme or arrangement or in any other manner or lending in any manner;
- such other non-banking institution or class of such institutions, as the bank may, specify with the previous approval of the Central Government and by notification in the Official Gazette

(ii) "Deposit taking non-banking financial company" means a non-banking financial company which is accepting or holding public deposits and is registered with the Reserve Bank of India under the provisions of the Reserve Bank of India Act, 1934.

(iii) "Systemically important non-deposit taking non-banking financial company" means a non-banking financial company which is not accepting or holding public deposits and having total assets of not less than Rs.500 crore as per the last audited balance sheet and is registered with the Reserve Bank of India under the provisions of the Reserve Bank of India Act, 1934.

(vi) Any sum payable by the assessee as interest on any loan or advances from -a scheduled bank or a co-operative bank other than a primary agricultural credit society or a primary co-operative agricultural and rural development bank in accordance with the terms and conditions of the agreement governing such loan or advance;

(vii) Any sum payable by the assessee as an employer in lieu of any leave at the credit of his employee; or (Leave Encashment)

(viii) Any sum payable by the assessee to the Indian Railways for the use of railway assets.

Manner of deduction: The expenditure shall be allowed as deduction in the following manner —

| Case | Year of allowance |
|--|--|
| If the sum relates to any previous year for which payment has been made on or before the due date of furnishing the return of income of that year. | In the previous year to which it relates |
| In any other case | In that year of payment |

In case of conversion of interest into loan / borrowing / advance: In case if any interest is payable covered under (d), (e) and (f) above and such interest is converted into loan or borrowing or advance, then the same shall not be allowed as deduction in the year of conversion, but shall be allowed in the year in which such converted loan is as actually paid.

Question 25: An analysis of the profit and loss account and the balance sheet of Kapil as at 31st March, 2023 reveals that the following expenses which were due, were through debited to the profit and loss account, but have been paid after 31st March, 2023:

- (i) **Goods and Services Tax:** Rs.50,000 (Rs.20,000 paid on 14th September, 2023; and Rs.30,000 paid on 15th December, 2023)
- (ii) **Customs duty:** Rs.1,20,000 (Rs.40,000 paid on 14th September, 2023; Rs.40,000 paid on 15th December, 2023 and Rs.40,000 paid on 24th December, 2023)
- (iii) **Bonus to staff:** Rs.60,000 (Rs.58,000 paid on 10th September, 2023, & Rs.2,000 paid on 15th December, 2023)
- (iv) **Employer's contribution to provident fund:** Rs.55,000 (Rs.25,000 paid on 15th July 2023; Rs.10,000 paid on 30th September, 2023; and Rs.20,000 paid on 15th December, 2023).
- (v) **Interest on term loan-from cooperative bank:** Rs.1,50,000 (Rs.1,20,000 paid on 14th July, 2023; and Rs.30,000 paid on 15th December, 2023).

The due date for filing of return is 31st October, 2023. In which previous years can the above payments be claimed as a deduction?

Solution: The aforesaid amounts shall be deductible as follows —

| Expenses | Amount of Expenditure | Date of payment | Amount of payment | Previous year in which deductible |
|-------------------------------|-----------------------|-----------------|-------------------|-----------------------------------|
| Goods and Services Tax | 50,000 | 14-09-2023 | 20,000 | 2022-23 |
| | | 15-12-2023 | 30,000 | 2023-24 |
| Customs duty | 1,20,000 | 14-09-2023 | 40,000 | 2022-23 |
| | | 15-12-2023 | 40,000 | 2023-24 |
| | | 24-12-2023 | 40,000 | 2023-24 |
| Bonus to staff | 60,000 | 10-09-2023 | 58,000 | 2022-23 |
| | | 15-12-2023 | 2,000 | 2023-24 |
| Employer's contribution to PF | 55,000 | 15-07-2023 | 25,000 | 2022-23 |
| | | 30-09-2023 | 10,000 | 2022-23 |
| | | 15-12-2023 | 20,000 | 2022-24 |

| | | | | |
|---|----------|------------|----------|---------|
| Interest on term loan from cooperative bank | 1,50,000 | 14-07-2023 | 1,20,000 | 2022-23 |
| | | 15-12-2023 | 30,000 | 2023-24 |

SPECIAL PROVISIONS / DEDUCTIONS

Special provision for full value of consideration for transfer of assets other than capital assets in certain cases [Section 43CA]: The said provisions are as under —

1. Stamp duty value deemed to be Full Value of consideration: Where 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 value adopted or assessed or assessable by any authority of a State Government for the purpose of payment of stamp duty in respect of such transfer, the value so adopted or assessed or assessable shall, for the purposes of computing profits and gains from transfer of such asset, be deemed to be the full value of the consideration received or accruing as a result of such transfer. However, where the value adopted or assessed or assessable by the authority for the purpose of payment of stamp duty does not exceed 110% of the consideration received or accruing as a result of the transfer, the consideration so received or accruing as a result of the transfer shall, for the purposes of computing profits and gains from transfer of such asset, be deemed to be the full value of the consideration.

In case of transfer of an asset, being a residential unit, 120% shall be taken instead of 110%, if the following conditions are satisfied, namely —

- (i) the transfer of such residential unit takes place during the period beginning from 12-11-2020 and ending on 30-06-2021;
- (ii) such transfer is by way of first time allotment of the residential unit to any person; and
- (iii) the consideration received or accruing as a result of such transfer does not exceed 2 crore.

[Amended by Finance Act, 2021 w.e.f. 01-04-2021 i.e. AY 2021-22)

“Residential unit” means an independent housing unit with separate facilities for living, cooking and sanitary requirement, distinctly separated from other residential units within the building, which is directly accessible from an outer door or through an interior door in a shared hallway and not by walking through the living space of another household.

2. Stamp duty value on the date of agreement to be considered: 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 full value of consideration may be taken to be the stamp duty value on the date of the agreement for such transfer and not on the date of registration of such transfer.

However, this provision shall apply only in a case where the amount of consideration or a part thereof has been received by way of an account payee cheque or an account payee bank draft or by use of electronic clearing system through a bank account or through such other electronic mode as may be prescribed, on or before the date of agreement for transfer of the asset. [(a) Credit Card; (b) Debit Card; (c) Net Banking; (d) IMPS (Immediate Payment Service); (e) UPI (Unified Payment Interface); (f) RTGS (Real Time Gross Settlement); (g) NEFT (National Electronic Funds transfer), and (h) BHIM (Bharat interface for Money) Aadhar Pay have been prescribed as mode of electronic payment]

3. Other provisions of Section 50C applicable: The other provisions of Section 50C shall be applicable for operation of Section 43CA.

Question: 26 – Section 43CA: Find out “full value of consideration” for the purpose of Section 43CA in the cases given below -

| Different Cases | Stamp duty value (date of agreement) | | Stamp duty value (date of agreement) | | Amount of consideration as per agreement | Date when first payment is received by seller by account payee cheque / draft, etc. |
|-----------------|--------------------------------------|------------|--------------------------------------|------------|--|---|
| | (Rs.) | Date | (Rs.) | Date | | |
| Case 1 | 26,40,000 | 15.07.2022 | 35,00,000 | 30.07.2022 | 24,00,000 | 10.07.2022 |
| Case 2 | 27,00,000 | 10.07.2022 | 35,00,000 | 30.07.2022 | 24,00,000 | 10.07.2022 |
| Case 3 | 25,00,000 | 15.07.2022 | 35,00,000 | 30.08.2022 | 24,00,000 | 10.08.2022 |
| Case 4 | 30,00,000 | 10.08.2022 | 31,50,000 | 30.08.2022 | 30,00,000 | 14.08.2022 |

Solution: Computation of Full value of consideration (amount in Rs.)

| Different Cases | Amount of consideration as per agreement | Stamp duty value (date of agreement) | | 110% of amount of consideration as per agreement | Full value of consideration u/s 43CA [if Column 4 is more than Column 5, Column 4 value will be taken, otherwise section 43CA, is not applicable] |
|-----------------|--|--------------------------------------|-----------|--|---|
| (1) | (2) | (3) | (4) | (5) | (6) |
| Case 1 | 24,00,000 | Date of agreement | 26,40,000 | 26,40,000 | 24,00,000 |
| Case 2 | 24,00,000 | Date of agreement | 27,00,000 | 26,40,000 | 27,00,000 |
| Case 3 | 24,00,000 | Date of agreement | 35,00,000 | 26,40,000 | 35,00,000 |
| Case 4 | 30,00,000 | Date of agreement | 31,50,000 | 33,00,000 | 30,00,000 |

ACCOUNTS AND AUDIT – SECTION 44AA & 44AB

Maintenance of books of accounts by certain persons carrying on business or profession [Section 44AA]:

1. Persons carrying on specified professions: Every person carrying on legal, medical, engineering or architectural profession or the profession of accountancy or technical consultancy or interior decoration or authorised representative or film artist or any other profession as is notified by the Board in the Official Gazette shall keep and maintain specified books of account and other documents,—

- (a) if his gross receipts exceeds Rs.1,50,000 in all of the three immediately preceding previous years or;
- (b) where the profession is newly setup, the gross receipts are likely to exceed 1,50,000 during current previous year.

Books of account to be maintained:

- (i) Cash book;
- (ii) Journal, in case of mercantile system of accounting;
- (iii) Ledger;
- (iv) Carbon copies or counterfoils of bills or receipts issued by him exceeding Rs.25;
- (v) Original bills issued to him and receipts in respect of expenditure incurred by him. In absence of bills, and where the payment does not exceed Rs.50, payment vouchers.

Additional books in case of medical profession: In case of medical profession following additional books are required to be maintained —

- (i) A daily case register in Form No. 3C;
- (ii) An inventory [under broad heads] as on the first and the last day of previous year, of the stock of drugs, medicines and other consumable accessories used for the purpose of his profession.

2. Other assessee's: The assessee's, other than those covered by (1) above, shall 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, —

| | |
|--|---|
| In case of existing business or profession | If - (a) his income from business or profession exceeds Rs.1,20,000; (Rs.2,50,000 in case of Individual or Hindu Undivided Family); or (b) Total sales / turnover / gross receipts thereof exceeds Rs.10,00,000 (Rs.25,00,000 in case of Individual or Hindu Undivided Family), in any of the three previous years immediately preceding the previous year. |
| In case of newly set up business or profession | If - (a) his income from business or profession is likely to exceed Rs.1,20,000 (Rs.2,50,000 in case of Individual or Hindu Undivided Family) during such previous year. (b) Total sales, turnover or gross receipts thereof is likely to exceed Rs.10,00,000 (Rs.25,00,000 in case of Individual or Hindu Undivided Family) during such previous year. |
| In case of deemed profits u/s 44AE, 44BB or 44BBB | If the assessee has claimed his income lower than the profits and gains so deemed, during such previous year. |
| Where the provisions of Section 44AD(4) are applicable | If his income exceeds the maximum amount which is not chargeable to income-tax in any previous year. |

Notes:

- (i) **Place at which books to be kept:** If the business is carried on at more than one place, then the books are to be kept at the principal place of profession. However, if separate books of accounts are maintained for each place of business, then the same are to be kept at the respective places, where profession is carried on.

(ii) Period for maintenance of books: The books of accounts are to be kept and maintained for a period of six years from the end of the relevant assessment year.

Question 27: Maintenance of books of Accounts: Vinod is a person carrying on profession as film artist. His gross receipt from profession are as under: -

| | |
|------------------------|-------------|
| Financial Year 2020-21 | Rs.1,15,000 |
| Financial Year 2021-22 | Rs.1,80,000 |
| Financial Year 2022-23 | Rs.2,10,000 |

What is his obligation regarding maintenance of books of accounts for each assessment year under Section 44AA of income-tax Act, 1961? **(5 Marks, May 2001, May 2008)**

Solution: Every person carrying on the profession of film artist shall keep and maintain specified books of account and other documents, if his gross receipts exceeds Rs.1,50,000 in all of the three immediately preceding previous years, since Mr. Vinod is a film artist he is required to maintain books of account only if his gross receipts exceeds Rs.1,50,000 in all of the 3 immediately preceding previous years. Accordingly -

| | |
|------------------------|---|
| Financial year 2020-21 | He is not required to maintain any books of accounts. |
| Financial year 2021-22 | He is not required to maintain any books of accounts. |
| Financial year 2022-23 | He is not required to maintain any books of accounts. |

Audit of accounts of certain persons carrying on business or profession [Section 44AB]

(1) Tax Audit: Every person shall get his accounts of any previous year audited by a Chartered Accountant before the specified date and furnish by that date the audit report in form 3CB along with prescribed particulars (Form 3CD).

| | |
|-----------------------|--|
| In case of Business | <p>his total sales, turnover or gross receipts, as the case may be, exceeds Rs.1 crore in any previous year;</p> <p>However; in the case of a person whose -</p> <p>(a) aggregate of all amounts received including amount received for sales, turnover or gross receipts during the previous year, in cash, does not exceed 50% of the said amount; and</p> <p>(b) aggregate of all payments made including amount received incurred for expenditure, in cash, during the previous year does not exceed 5% of the said payment,</p> <p>he will have to get his accounts audited if his total sales, turnover or gross receipts, as the case may be, exceeds Rs.10 crore in any previous year;</p> <p>The payment or receipt, as the case may be, by a cheque drawn on a bank or by a bank draft, which is not account payee, shall be deemed to be the payment or receipt, as the case may be, in cash.</p> |
| In case of Profession | his gross receipts exceeds Rs.50 lakhs in any previous year; or |

| | |
|---|--|
| In case the profits and gains from the business are deemed profits u/s 44AE, 44BB or 44BBB | he has claimed his income to be lower than the profits or gains so deemed in any previous year; or |
| In case the profits and gains from the profession are deemed profits u/s 44ADA | he has claimed his income to be lower than the profits and gains so deemed and his income exceeds the maximum amount not chargeable to tax in any previous year or |
| In case of business if the provisions of section 44AD(4) are applicable in his case | his income exceeds the maximum amount which is not chargeable to income-tax in any previous year. |
| “Specified date”, in relation to the accounts of the assessee of the previous year relevant to an assessment year, means date one month prior to the due date for furnishing the return of income under Section 139(1). | |

- (2) **Non-applicability:** This section shall not apply to the person, who declares profits and gains for the previous year in accordance with the provisions of Section 44AD(1) and his total sales, turnover or gross receipts, as the case may be, in business does not exceed Rs.2 crore in such previous year
- (3) **Audit under other law:** In case where such person is required 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 due date for furnishing the return of income under section 139(1) and furnishes the audit report by that date in Form 3CA along with prescribed particulars (Form 3CD).

DEEMED PROFITS INCASE OF CERTAIN BUSINESSES – SECTION 44AD, 44ADA & 44AE

Special provision for computing profits and gains of business on presumptive basis [Section 44AD]:

1. **“Eligible assessee”** means,—
 - (i) an individual, Hindu undivided family or a partnership firm, who is a resident, but not a limited liability partnership firm; and
 - (ii) who has not claimed deduction under any of the sections 10A, 10AA, 10B, 10BA or deduction under any provisions of sections 80-IA to 80-RRB in the relevant assessment year.
2. **“Eligible business”** means,—
 - (i) any business except the business of plying, hiring or leasing goods carriages referred to in section 44AE; and
 - (ii) whose total turnover or gross receipts in the previous year does not exceed an amount of Rs.2 crore.
3. **Non-applicability:** The provisions of this section shall not apply to —
 - (i) a person carrying on specified profession as referred to section 44AA i.e. legal, medical, engineering or architectural profession or the profession of accountancy or technical consultancy or interior decoration or any other profession as is notified by the Board (film artists, company secretaries, etc.);
 - (ii) a person earning income in the nature of commission or brokerage; or
 - (iii) a person carrying on any agency business.

- 4. Presumptive Income:** Notwithstanding anything to the contrary contained in sections 28 to 43C, in case of an eligible assessee engaged in an eligible business —
- (i) a sum equal to 8% of the total turnover or gross receipts of the assessee in the previous year on account of such business (6% of the amount of total turnover or gross receipts which is received by an account payee cheque or an account payee bank draft or use of electronic clearing system through a bank account or through such other electronic mode as may be prescribed during the previous year or before the due date specified in Section 139(1) in respect of that previous year); [(a) Credit Card; (b) Debit Card (c) Net Banking; (d) IMPS (Immediate Payment Service); (e) UPI (Unified Payment interface); (f) RTGS (Real Time Gross Settlement); (g) NEFT (National Electronic Funds Transfer), and (h) BHIM (Bharat Interface for Money) Aadhar Pay have been prescribed as mode of electronic payment) or
 - (ii) a sum higher than the aforesaid sum claimed to have been earned by the eligible assessee; 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”.
- 5. No deductions under section 30 to 38:** Any deduction allowable under the provisions of Sections 30 to 38 (including unabsorbed depreciation, unabsorbed capital expenditure on scientific research / family planning) shall be deemed to have been already deducted and no further deduction under those sections shall be allowed.
- 6. Determination of WDV of assets:** The WDV of any asset of an eligible business shall be deemed to have been calculated as if the assessee had claimed and had been actually allowed the deduction in respect of the depreciation for each of the relevant assessment years.
- 7. Consequences of declaring lower income [Section 44AD(4)]:** Where an eligible assessee declares profit for any previous year in accordance with the provisions of this section and he declares profit for any of the 5 subsequent assessment years i.e. subsequent to the assessment year relevant to the previous year in which profit has not been declared at rate of 8%, then he shall not be eligible to claim the benefit of the provisions of this section for 5 assessment years subsequent to the assessment year relevant to the previous year in which the profit has not been declared at rate of 8%.
- 8. In case profits claimed to be lower than the deemed profits — Maintenance of accounts and audit:**
An eligible assessee
- (a) to whom the provisions of Section 44AD(4) as discussed above are applicable; and
 - (b) whose total income exceeds the maximum amount which is not chargeable to income-tax, shall be required to keep and maintain such books of account and other documents as required under section 44AA(2) and get them audited and furnish a report of such audit as required under section 44AB.
- 9. Advance tax to be deposited upto 15th March of the relevant year:** An eligible assessee in respect of an eligible business referred to in section 44A1), to the extent of the whole amount of such advance tax during each financial year on or before the 15th March.
- 10. In case of supply of materials by contractee / purchaser - No profit is earned thereon by contractor / manufacturer, hence not includible in turnover / gross receipts [Brij Bhushan Lal Praduman Kumar v. CIT [1978] 115 ITR 524 (SC)]:** If the material is supplied by the purchaser/contractee to the

contractor/manufacturer-seller, then such materials supplied always remain the property of the purchaser / contractee. Hence, it is impossible that there is any element of profit being involved in the turnover represented by the cost of such materials.

Thus, where materials are supplied to the contractor solely to use, fix or incorporate in the works, value of the entire contract = Value - Cost of materials so supplied.

Accordingly, the profits from such contracts are to be determined on the basis of the value of the contract represented by the cash payments received by the contractor as excluding the cost of the materials so supplied by the purchaser / contractee,

Question 28: Presumptive basis taxation Section 44AD: Mr. Praveen engaged in retail trade, reports a turnover of Rs.1,58,50,000 (out of which Rs.1,00,00,000 is received through account payee cheque) for the financial year 2022-23. His income from the said business as per books of account is computed at Rs.6,90,000. Retail trade is the only source of income for Mr. Praveen.

- i) Is Mr. Praveen eligible to opt for presumptive determination of his income chargeable to tax?
- ii) If so, determine his income from retail trade as per the applicable presumptive provision.
- iii) In case, Mr. Praveen does not opt for presumptive taxation of income from retail trade, what are his obligations under the Income-tax Act, 1961?
- iv) What is the 'due date' for filing his return of income, under both the options?

(5 Marks, PCC May 2011)

Solution: Thus, the relevant answers are as follows —

- i) Yes. Mr. Praveen is an individual and the turnover of his business is not more than Rs.200 lakhs. Hence, Section 44AD applies to him and his income shall be computed as per section 44AD.
- ii) His Income from retail trade u/s 44AD 6% of turnover of Rs.1,00,00,000 + 8% of turnover of Rs.58,50,000 = Rs.10,68,000.
- iii) In case he opts Out of section 44AD and claim that his profits are only Rs.6,90,000 (which is lower than presumptive income of Rs.10,68,000), then he has to maintain requisite books of account as required in section 44AA and gets them audited under section 44A8.
- iv) If he accepts presumptive income under section 44AD, then, the due date of return of income is 31.7.2023, for the assessment year 2023-24. However, if he decides that provision of said section is not made applicable then he will have to gets his accounts audited, then, the due date shall be **31.10.2023**.

The special provision for computing profits and gains of profession on presumptive basis as per Section 44ADA.

Ans: Special provision for computing profits and gains of profession on presumptive basis [Section 44ADA]

1. Eligible Assessee: The eligible assessee is an assessee,

- (a) being an individual or a partnership firm other than a limited liability partnership, who is a resident in India,
- (b) who is engaged in a profession referred to in Section 44A A (1); and
- (c) whose total gross receipts do not exceed Rs.50 lakh in a previous year.

2. Presumptive Income: The deemed profits and gains of such profession chargeable to tax under the head "Profits and gains of business or profession" shall be —
 - (a) A sum equal to 50% of the total gross receipts of the assessee in the previous year on account of such profession; or
 - (b) a sum higher than the aforesaid sum claimed to have been earned by the assessee.
3. **No further deduction:** Any deduction 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 from such deemed income,
4. **WDV of Assets:** The written down value of any asset used for the purposes of profession shall be deemed to have been calculated as if the assessee had claimed and had been actually allowed the deduction in respect of the depreciation for each of the relevant assessment years.
5. Accounts and audit if profits claimed to lower than deemed profits : Notwithstanding anything contained in the foregoing provisions of this section,—
 - (a) an assessee who claims that his profits and gains from the profession are lower than the deemed profits and gains specified above, and
 - (b) whose total income exceeds the maximum amount which is not chargeable to income-tax, shall be required to keep and maintain such books of account and other documents as required under section 44AA(i) and get them audited and furnish a report of such audit as required under section 44AB.
6. **Advance Tax:** Further, since the presumptive taxation regime has been extended for professionals also, the eligible assessee is now required to pay advance tax by 15th March of the financial year.

Question 29: Presumptive basis u/s 44ADA: Ms Kriti is a Chartered Accountant in practice. She maintains her accounts on cash basis. Her Income and Expenditure account for the year ended 31st March, 2023 as follows

| Expenditure | Rs. | Income | Rs. | Rs. |
|---|------------------|--|-----------|------------------|
| Salary to staff | 5,50,000 | Fees earned | | |
| Stipend to articled assistants | | - Audit | 17,88,000 | |
| Incentive to articled assistants | 37,000 | - Taxation services | 5,40,300 | |
| Office rent | | - Consultancy | 2,70,000 | 25,98,300 |
| Printing and stationery | 3,000 | Dividend on shares of Indian | | |
| Meeting seminar and conference | 24,000 | companies (Gross) | | 10,524 |
| | 22,000 | Income from units of mutual | | S. |
| Purchase of car | 31,600 | funds (Gross) | | 7,600 |
| Repair, maintenance and petrol of car | 80,000 | Honorarium received from various institutions for valuation of answer papers | | 1,800 |
| | 4,000 | Rent received from residential flat let out | | 85,600 |
| Travelling expenses- | 35,000 | | | |
| Municipal tax paid in respect of house property | 3,000 | | | |
| Net Profit | 19,28,224 | | | |
| | 27,17,824 | | | 27,17,824 |

Other Information:

- (i) Allowable rate of depreciation on motor car is 15%
- (ii) Incentives to articled assistants represent amount paid to two articled assistants for passing IPCC Examination
- (iii) Salary include Rs.15,000 to a computer specialist in cash on 15.07.2022 for assisting Ms. Kriti in one professional assignment.

On the basis of above information, determine whether Ms. Kriti should opt for presumptive basis taxation for computation of her Gross Total Income for assessment year 2023-24.

Solution: Computation of the Gross Total Income for the assessment year 2023-24.

- **CASE I:** When Ms. Kriti opt for the provisions of Section 44ADA:

Computation of gross total income (amounts in Rs.):

| | | |
|---|--------|------------------|
| Income from house property: | | |
| Actual Rent Received [Being Gross Annual Value u/s 23(1)] | 85,600 | |
| Less: Municipal taxes paid | 3,000 | |
| Net Annual Value (NAV) | 82,600 | |
| Less: Standard deduction u/s 24 @ 30% of NAV | 24,780 | 57,820 |
| Income under the head Profits & Gains of Business and Profession | | |
| 50% of the Gross receipts i.e. 50% of 25,98,300 is deemed profits from profession under Section 44ADA | | 12,99,150 |
| Income from other sources: | | |
| Dividends from Indian companies [Taxable in hands of shareholder] | 10,524 | |
| Income from Unit Trust of India. [Taxable in hands of unit holder] | 7,600 | |
| Honorarium for valuation of answer papers | 15,800 | 33,924 |
| Gross Total Income | | 13,90,894 |

- **CASE II:** When income is computed as per normal provisions of the Act.

Computation of gross total income (amounts in Rs.):

| | | |
|---|---------------|--------|
| Income from house property: | | |
| Actual Rent Received [Being Gross Annual Value u/s 23(1)] | 85,600 | |
| Less: Municipal taxes paid | <u>3,000</u> | |
| Net Annual Value (NAV) | 82,600 | |
| Less: Standard deduction u/s 24 @ 30% of NAV | <u>24,780</u> | 57,820 |
| Income under the head Profits & Gains of Business and Profession | | |
| Net profit as per Income and Expenditure Account | 19,28,224 | |
| Add: Expenses debited hut not allowable | | |
| Municipal Taxes of house property in respect of residential flat let out | 3,000 | |
| Salary paid to computer specialist in cash disallowed u/s 40A(3), since such cash payment is in excess of Rs.10,000 | 15,000 | |
| Amount paid for purchase of car is not allowable u/s 37(1) since it is a capital expenditure | 80,000 | |

| | | |
|--|---------------|------------------|
| Less: Income credited but not taxable under this head | | |
| Dividend on shares of Indian Companies [The same taxable under the head Income From Other Sources] | 10,524 | |
| Income from Unit Trust of India. [The same taxable under the head Income From Other Sources I | 7,600 | |
| Honorarium for valuation of answer papers [The same is taxable under the head 'Income from other sources'] | 15,800 | |
| Rent received from residential flat let out [The same is taxable under the 'Income from house property] | 85,600 | |
| Depreciation on Motor Car @ 15% [WNI | <u>12,000</u> | 18,94,700 |
| Income from other sources: | | |
| Dividends from Indian companies [Taxable in hands of shareholder] | 10,524 | |
| Income from Unit Trust of India. [Taxable in hands of shareholder] | 7,600 | |
| Honorarium for valuation of answer papers | 15,800 | 33,924 |
| Gross Total Income | | 19,86,444 |

Working Note: It has been assumed that the motor car was put to use for more than 180 days during the previous year and hence, full depreciation @ 15% has been provided for under section 32(1)(ii).

Conclusion: The assessee should opt for the provisions of Section 44ADA since her income from profession as per the said section is Rs.12,99,150 which is less than actual income of Rs.18,94,700.

Special provision for computing profits and gains of business of plying, hiring or leasing goods carriages [Section 44AE]:

1. Eligible assessee: Notwithstanding anything to the contrary contained in Sections 28 to 43C, in the case of an assessee who —

(i) owns not more than 10 goods carriages at any time during the previous year; and

(ii) 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 profits, from all the goods carriages owned by him in the previous year.

Hire purchaser deemed to be the owner of goods carriage: An assessee, who is in possession of a goods carriage, whether taken on hire purchase or on installments and for which the whole or part of the amount payable is still due, shall be deemed to be the owner of such goods carriage.

Note: Even if on a single day, the number of goods carriages (whether heavy goods vehicle or not) exceeds 10, then, this section shall not apply to that assessee for that previous year.

2. Deemed Profits: The income chargeable to tax under the head "Profits and gains of business or profession" from such business shall be computed as follows —

| | Particulars | Rs. |
|----|---|-----|
| I. | In case of goods carriage being a heavy goods vehicle Higher of — (a) Rs.1,000 per ton of gross vehicle weight or unladen weight, as the case may be, per month per vehicle x No. of month(s) or part of a month in the previous year during which the heavy vehicle is owned by the assessee x No. of heavy goods Vehicle | xx |

| | | |
|---|--|-----------|
| | (b) An amount claimed to have been actually earned from such vehicle(s) | |
| II. | In case of goods carriage other than a heavy goods vehicle Higher of - (a) Rs.7,500 per month per vehicle x No. of month(s) or part of a month in the previous year during which the vehicle is owned by the assessee x No. of other goods carriages (b) An amount claimed to have been actually earned from such vehicle(s) | xx |
| Profits & Gains of Business or Profession from this business (I + II) | | xx |
| “ Heavy goods vehicle ” means any goods carriage, the gross vehicle weight of which exceeds 12000 kilograms. | | |
| “ Gross vehicle weight ” means total weight of the vehicle and load certified and registered by the registering authority as permissible for that vehicle. | | |
| “ Unladen weight ” means the weight of a vehicle or trailer including all equipment ordinarily used with the vehicle or trailer when working but excluding the weight of driver or attendant and where alternative parts or bodies are used the unladen weight of the vehicle means the weight of the vehicle with the heaviest such alternative body or part. | | |

3. **All other deduction deemed to be allowed:** The assessee will be deemed to have been allowed the deductions under sections 30 to 38 Accordingly, the written down value of any asset used for the purpose of the business of the assessee will be deemed to have been calculated as if the assessee had claimed and had actually been allowed the deduction in respect of depreciation for each of the relevant assessment years.
4. **Salary and interest to partners is allowed:** Where the assessee is a firm, the salary and interest paid to its partner are allowed to be deducted subject to the conditions and limit specified under section 40(b).
5. **Not requirement to maintain books of accounts and get the accounts audited:** The assessee joining the scheme will not be required to maintain books of account under section 44AA and get the accounts audited under section 44AB in respect of such income.
6. **Option to claim lower profits:** An assessee may claim lower profits and gains than the deemed profits and gains specified in Section 44AE(1) of that section select to the condition that the books of account and other documents are kept and maintained as required under section 44AA(2) and the assessee gets his accounts audited and furnishes a report of such audit as required under section 44AB.

AGRICULTURAL INCOME

Section 10(1) exempts ‘agricultural income’ from income tax chargeable under this Act. However, it is chargeable to income-tax at state-level as per state laws. As per section 2(A), agricultural income means

1. **Rent or Revenue derived from land [Section 2(1A)(a)]:** Any rent or revenue should be derived from land, which is situated in India and is used for agricultural purposes.

The amount received in money or in kind, by one person from another for right to use land is termed as Rent. The rent can either be received by the owner of the land or by the original tenant from the sub-tenant. It implies that ownership of land is not necessary. Thus, the rent received by the original tenant from sub-tenant would also be agricultural income subject the other conditions mentioned above.

The scope of the term “Revenue” is much broader than rent. It includes income other than rent. For example, fees received for renewal for grant of land on lease would be revenue derived from land. The Supreme Court in CIT v. Raja Benoy Kumar Sahas Roy, has held that, agricultural activity is divided into two parts:

(i) Basic operations: It means application of human skill & labour upon the land, prior to germination E.g. Tilling, sowing, planting and similar operations.

(ii) Subsequent operations: It means operations which fosters the growth and preserves the produce, for rendering the produce fit for sale in market, and which are performed after the produce sprouts from the land, like weeding, digging the soil, removal of undesirable undergrowth’s, prevention of crop from insects and pests, depredation from outside, cutting, pruning etc.

Both basic and subsequent operations are to be performed to constitute agriculturist activities.

One cannot disassociate the basic operations from the subsequent operations.

2. Income derived from agricultural land by agricultural operations [Section 2(1A)(b)]: This includes -

(i) Income derived from such land by agriculture.

(ii) Income derived by cultivator or receiver of rent in kind, for any process ordinarily employed to render the produce raised, fit to be taken to the market.

(iii) Income derived from sale of agricultural produce is also agricultural income.

3. Income from farm building [Section 2(1A)(c)]: if a building satisfies the following conditions, then income from such building shall be treated as agricultural income —

(i) Building must be occupied by the cultivator or receiver of rent in kind;

(ii) It is on or in the immediate vicinity of land situated in India and used for agricultural purposes;

(iii) The building is occupied as a dwelling house, storehouse or other out-building; and

(iv) Land is either assessed to land revenue or local rate, or it is situated in a rural area**.

****Note:** “Rural area” means any area which is outside the jurisdiction of a municipality or a cantonment board and which has a population of 10,000 or more and which does not fall within distance (to be measured aerially) given below —

| | |
|---|---|
| ➤ 2 kilometres, from the local limits of any municipality or cantonment board | ➤ If the population of municipality or cantonment board is more than 10,000 but not exceeding 1,00,000; or |
| ➤ 8 kilometres, from the local limits of any municipality or cantonment board | ➤ If the population of municipality or cantonment board is more than 1,00,000 but not exceeding 10,00,000; or |
| ➤ 8 kilometres, from the local limits of any municipality or cantonment board | ➤ If the population of municipality or cantonment board is more than 10,00,000. |

“Population” means the population according to the last preceding census of which the relevant figures have been published before the first day of the previous year. [Explanation]

4. **Surplus from transfer of urban agricultural land [Explanation 1]:** Any surplus arising from transfer of “urban agricultural land” is not treated as revenue derived from land.
5. **Income from non-agricultural use of farm-building — Not agricultural income [Explanation 2]:** However, income derived from any such building or land from its use for non-agricultural purposes (including letting for residential purpose or for the purpose of any business or profession) shall not be agricultural income.
6. **Income from plant nursery - Deemed agricultural income [Explanation 3]:** Any income derived from saplings or seedlings grown in a nursery shall be deemed to be agricultural income.

Question 30: Give instances of agricultural income and non-agricultural income.

Ans: Instances of agricultural income:

1. Income from growing trade or commercial products like jute, cotton, etc. is an agricultural income.
2. Income from growing flowers is an agricultural income,
3. Plants sold in pots are an agricultural income provided basis operations are performed.
4. Remuneration and interest to partner: Any remuneration (salary, commission, etc.) received by partner from a firm engaged in agricultural operation is an agricultural income.
Interest on capital received by a partner from a firm engaged in agricultural operation is an agricultural income.

Instances of Non-agricultural Income:

1. Salary received by an employee from any business (having agricultural income),
2. Dividend received from a company engaged in agricultural operation.
3. Income from fisheries.
4. Income from poultry farming.
5. Income from dairy farming, butter & cheese making, etc..
6. Breeding & rearing of livestock.
7. Income earned by a cultivator from conversion of sugarcane (raised on own land) to jaggery is non-agricultural income to the extent to which income is related to such conversion only. This is because sugarcane itself is marketable.
8. Income from a land situated outside India is non-agricultural income and taxable under the head “Income from other sources”.
9. Income from sale of trees and, grasses grown spontaneously (without any human effort).
10. Proceeds from sale of cocoons are not agricultural income. Here, assessee grows mulberry leaves and rears silkworms, and then sells the silk cocoons in the market. Therefore agricultural produce of the cultivator will be mulberry leaves and the silkworms cannot be regarded as the agricultural produce of the cultivator. **K. Lakshmanan & Co. v. CIT [2000] 239 ITR 597 (SC).**

Question 31: Give the’ disintegration of income in case of - (A) Rubber, coffee and tea business. (B)

Any other business

Ans: Disintegration of income is as follows —

(A) in case of rubber, coffee and tea business

| Particulars | Rubber [Rule 7A] | Coffee [Rule 7B] | | Tea [Rule 8] |
|-----------------------------------|--|---|--|---|
| Income derived from the sale of - | Latex/ cenex / block rubbers manufactured or processed from rubber plants grown by seller in India | Coffee grown & cured by seller in India | Coffee grown, cured, roasted and grounded by seller in India | Tea grown & manufactured by seller in India |
| Business income | 35% | 25% | 40% | 40% |
| Agricultural income | 65% | 75% | 60% | 60% |

(B) In case of any other business (Rule 7) : The following mode will be adopted

(a) Agricultural Income = (Market value of agricultural produce used as raw material for business + Sale proceeds from direct sale of agricultural produce) – Cost of Cultivation.

(b) Business Income = Sale proceeds of the processed goods - Market value of agricultural produce used as raw material for business - Expenses for processing.

Question 32: Computation of Business and agricultural Income: Mr. Tony had estates-in Rubber, Tea- and Coffee. He derives income from them He has also a nursery wherein he grows plants and sells. For the previous year ending 31.3.2022, he furnishes the following particulars of his sources of income from estates and sale of plants

(amounts in Rs.)

| | |
|--|----------|
| (a) Manufacture of Rubber | 5,00,000 |
| (b) Manufacture of Coffee grown and cured | 3,50,000 |
| (c) Manufacture of Tea | 7,00,000 |
| (d) Sale of plant from nursery | 1,00,000 |

You are requested to compute the taxable income. **(5 Marks, CA PE-II Nov. 2004).**

Solution: Computation of taxable income of Tony (amount in Rs.) -

| Total | Business income | Agricultural income |
|--|-----------------|---------------------|
| Income from growing and manufacturing rubber (Rule 7A) — 35% : 65% | 1,75,000 | 3,25,000 |
| Income from growing and curing coffee (Rule 7B) - 25% : 75% | 87,500 | 2,62,500 |
| Income from growing and manufacturing tea (Rule 8) - 40% : 60% | 2,80,000 | 4,20,000 |
| Sale of plants from nursery (it is an agricultural income) | Nil | 1,00,000 |
| Total | 5,42,500 | 11,07,500 |

Hence, total income of Mr. Tony = Rs.5,42,500.

Question 33: Computation of Business and agricultural Income: Miss. Kavita, a resident and ordinarily resident in India, has derived the following income for the year ended 31-3-2023:

| | Rs. |
|---|----------|
| (i) Income from sale of centrifuged latex processed from rubber plants grown in Darjeeling | 1,00,000 |
| (ii) Income from sale of coffee grown and cured in Yereaud, Tamil Nadu | 2,00,000 |
| (iii) Income from sale of coffee grown, cured, roasted and grounded in Colombo. Sale consideration was received in Chennai | 5,00,000 |

- (iv) Income from sale of tea grown and manufactured in Shimla 10,00,000
- (v) Income from sapling and seedling grown in a nursery at Cochin. Basic operations were not carried out by her on land. 2,00,000

You are required to compute the business income and agricultural income of Miss Kavita for the Assessment Year 2023-24. (5 Marks, May 2018) (Similar: 6 Marks, CA PE-II June, 2009)

Solution: Computation of taxable income of Miss Kavita (amounts in Rs.)

| Particulars | Business Income | Agricultural Income |
|--|-----------------|---------------------|
| Income from growing & manufacturing rubber in India (Rule 7A) - 35% : 65% | 35,000 | 65,000 |
| Income from growing and curing coffee in India (Rule 7B) - 25% : 75% | 50,000 | 1,50,000 |
| Income from growing/curing/roasting etc. coffee out of India in Colombo (Sri Lanka) [WN-1] | 5,00,000 | - |
| Income from growing and manufacturing tea in India (Rule 8) — 40% : 60% | 4,00,000 | 6,00,000 |
| Income from sapling and seedling grown in nursery [WN-2] | | 2,00,000 |
| Total | 9,85,000 | 10,15,000 |

Working Note:

- (1) Income from a land situated outside India is Non-Agricultural income. Since the operations have taken place outside India, hence, no part of such income can be regarded as agricultural income (Rule 7B will not apply). Since Miss Kavita is resident in India, hence, this income will be taxed in India.
- (2) Income from sapling and seedling grown in a nursery is deemed agricultural income even if no basic operations have been carried out.

Question 34: X Ltd. grows sugarcane to manufacture sugar. Details for the previous year 2022-23 are as follows:

| Particulars | Rs. in lacs. |
|---|--------------|
| Cost of cultivation of sugarcane (5,000 tons) | 10 |
| Sugarcane sold in market (1,000 tons) | 3 |
| Sugarcane used for sugar manufacturing (4,000 tons) | - |
| Cost of conversion | 5 |
| Sugar produced & sold in market | 25 |

Compute income of X Ltd.

Solution:

Computation of income of X Ltd. for the A.Y. 2023-24 Rs. in lacs

| Particulars | Manufacturing | Agriculture |
|--|---------------|-------------|
| Sale of agro product in market | - | 3 |
| Sale of manufactured product in market | 25 | - |
| Notional sale of agro product used in the process of manufacturing (4,000 ton × Rs. 3 lacs per '000 ton) | - | 12 |
| Revenue [A] | 25 | 15 |

| | | |
|--|----------|----------|
| Less: Expenses incurred | | |
| Cost of conversion | 5 | - |
| Market value of sugarcane used (4,000 ton × Rs. 3 lacs per '000 ton) | 12 | - |
| Cost of cultivation | - | 10 |
| Expenditure [B] | 17 | 10 |
| Income [A – B] | 8 | 5 |

Question 35: State the tax treatment of the following income -

- (a) A is employed in an agricultural farm and entrusted with tilling of land, his remuneration being 50% of the net profits earned by the farm.
- (b) C receives a dividend of Rs. 12,000 from a company whose entire income is derived from agricultural operations only.
- (c) D of Kolkata earns an income of Rs. 12,000 from agricultural land owned by him and situated in Bangladesh. Such income is received in Bangladesh.
- (d) F receives Rs. 600 on account of interest on loan on the mortgage of land which is used for agricultural purposes.
- (e) G earns an income of Rs. 1,200 from lease of land for grazing of cattle required for agricultural operations.
- (f) H receives Rs. 400 on account of interest on arrears of rent in respect of land used by tenant for agricultural operations.
- (g) Income from the sale of replanted trees where the denuded parts of the forest are replanted and subsequent operation in forestry are carried out.
- (h) Income from sale of trees of forest which are of spontaneous growth and in relation to which forestry operations alone are performed or Income from sale of wild grass of spontaneous growth
- (i) Income from sale of tea leaf from a tea garden.
- (j) Income from sale of jute produced in land situated in Bangladesh.
- (k) Income from poultry farming
- (l) Income from growing flowers in gardens
- (m) Income from sale of tobacco leaves after being dried to make it fit for sale.
- (n) Income from fisheries or poultry or dairy
- (o) Income of Rs. 50,000 from agricultural land, the land is situated in Bangladesh
- (p) Income of Rs. 25,000 from the land used as stone quarries.

Solution:

- (a) Since Mr. A is an employee of the concern, therefore his income shall be taxable under the head 'Salaries' and shall not be treated as agricultural income. However, if Mr. A is a partner of the concern then such income shall be treated as agricultural income.
- (b) Dividend received from a company (engaged in agricultural business) cannot be treated as agricultural income. Such dividend shall be taxable under the head "Income from other sources".
- (c) Any income from a land situated outside India is not an agro-income and taxable under the head

“Income from other sources”. It is to be noted that such income shall be taxable only if the assessee is an ordinarily resident in India.

- (d) Interest on loan on the mortgage of land used for agricultural purpose is not an agro-income.
- (e) Any rent derived from land used for grazing of cattle, used for agricultural operation, is an agro-income.
- (f) Interest on arrears of rent receivable in respect of agricultural land is non-agricultural income.
- (g) Assume replantation of trees has been done with application of basic operation on land. Hence such income is agro-income.
- (h) Income from sale of trees, grass grown spontaneously and without any human effort is non-agricultural income.
- (i) It will be treated as agricultural income.
- (j) Income from sale of jute produced in land situated in Bangladesh is not treated as agricultural income. For the purpose of this, land should be situated in India.
- (k) Income from Poultry farming is not an agricultural income because such income is not derived from land.
- (l) Income from growing flowers in garden is as an agricultural Income as the same is derived from a land by performing agricultural operations on it.
- (m) Income from sale of tobacco leaves after being dried to make it fit for sale is an agricultural income.
- (n) Income from fisheries or poultry or dairy is not considered as agricultural income as the same is not derived from land.
- (o) Since the land is situated outside India, hence income is not considered as agricultural income.
- (p) It is not an agricultural income as no agricultural operation has been carried on the land.

THE END