

INCOME TAX

Second Year : B.Com.

SEMESTER – IV

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2nd Year B.Com. Semester – IV

INCOME TAX

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Director

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FOREWORD

Since its establishment in 1976, Acharya Nagarjuna University has been forging ahead in the path of progress and dynamism, offering a variety of courses and research contributions. I am extremely happy that by gaining a 'A' Grade from the NAAC in the year 2014, the Acharya Nagarjuna University is offering educational opportunities at the UG, PG levels apart from research degrees to students from over 285 affiliated colleges spread over the two districts of Guntur and Prakasam.

The University has also started the Centre for Distance Education with the aim to bring higher education within reach of all. The centre will be a great help to those who cannot join in colleges, those who cannot afford the exorbitant fees as regular students, and even housewives desirous of pursuing higher studies. With the goal of bringing education in the door step of all such people. Acharya Nagarjuna University has started offering B.A, and B, Com courses at the Degree level and M.A, M.Com., L.L.M., courses at the PG level from the academic year 2021-22 on the basis of Semester system.

To facilitate easier understanding by students studying through the distance mode, these self-instruction materials have been prepared by eminent and experienced teachers. The lessons have been drafted with great care and expertise in the stipulated time by these teachers. Constructive ideas and scholarly suggestions are welcome from students and teachers invited respectively. Such ideas will be incorporated for the greater efficacy of this distance mode of education. For clarification of doubts and feedback, weekly classes and contact classes will be arranged at the UG and PG levels respectively.

It is aim that students getting higher education through the Centre for Distance Education should improve their qualification, have better employment opportunities and in turn facilitate the country's progress. It is my fond desire that in the years to come, the Centre for Distance Education will go from strength to strength in the form of new courses and by catering to larger number of people. My congratulations to all the Directors, Coordinators, Editors and Lesson -writers of the Centre who have helped in these endeavours.

Prof. P.Rajasekhar
Vice –Chancellor,
Acharya Nagarjuna University

PROGRAMME: THREE-YEAR B COM

(General and Computer Applications)

Course Code:

Domain Subject: Commerce

Semester-wise Syllabus under CBCS

(w.e.f. 2020-21 Admitted Batch)

II Year B Com (Gen& CA)– Semester – IV

403BCO21-**Course 4C:Income Tax**

Learning Outcomes:

At the end of the course, the student will able to;

- Acquire the complete knowledge of the tax evasion, tax avoidance and tax planning.
- Understand the provisions and compute income tax for various sources.
- Grasp amendments made from time to time in Finance Act.
- Compute total income and define tax complicacies and structure.
- Prepare and File IT returns of individual at his own.

Syllabus:

Unit-I: Introduction: Income Tax Act-1961 - Basic Concepts: Income, Person, Assessee - Assessment Year, Previous Year, Rates of Tax, Agricultural Income, Residential Status of Individual -Incidence of Tax – Incomes Exempt from Tax (theory only).

Unit-II: Income from Salaries: Basis of Charge, Tax Treatment of Different Types of Salaries Allowances, Perquisites, Profits in Lieu of Salary, Deductions from Salary Income, Computation of Salary Income (including problems).

Unit-III: Income from House Property and Profits and Gains from Business: Annual Value, Let-out/Self Occupied/Deemed to be Let-out house -Deductions from Annual Value - Computation of Income from House Property

Definition of Business and Profession – Procedure for Computation of Income from Business – Revenue and Capital Nature of Incomes and Expenses – Allowable Expenses – Expenses Expressly Disallowed – Computation (including problems).

Unit-IV: Income from Capital Gains - Income from Other Sources: Meaning of Capital Asset – Types – Procedure for Computation of Long-term and Short-term Capital Gains/Losses

Meaning of Other Sources - General Incomes – Specific Incomes – Computation (including problems).

Unit-V: Computation of Total Income of an Individual: Deductions under Section 80 - Computation of Total Income (Simple problems).

Reference Books:

1. Dr. Vinod; K. Singhanian; Direct Taxes – Law and Practice, Taxman Publications
2. T. S. Reddy and Dr. Y. Hari Prasad Reddy - Taxation , by Margham Publications
3. Premraj and Sreedhar, Income Tax, Hamsrala Publications
4. B.B. Lal - Direct Taxes; Konark Publications
5. Dr. Mehrotra and Dr. Goyal -Direct Taxes, Law and Practice, Sahitya Bhavan Publication.
6. Balachandran&Thothadri- Taxation Law and Practice, PHI Learning.
7. V.P. Gaur and D.B. Narang - Income Tax, Kalyani Publications
8. Dr Y Kiranmayi - Taxation, Jai Bharath Publishers
9. Income Tax, Seven Lecture Series, Himalaya Publications

Suggested Co-Curricular Activities:

- Seminar on different topics of Income tax
- Quiz programs
- Problem Solving Exercises
- Debate on Tax Evasion and Avoidance
- Practice of provisions of Taxation
- Visit a Tax firm
- Talk on Finance Bill at the time of Union Budget
- Guest lecture by Chartered Accountant
- Presentation of tax rates
- Practice of filing IT Returns online
- Group Discussions on problems relating to topics covered by syllabus
- Examinations (Scheduled and surprise tests)

MODEL QUESTION PAPER

(403BCO21)

B. Com.(General / Comp. Appl.s) Degree Examination

Second Year – Fourth Semester

Part – II : Commerce

Paper – IV : INCOME TAX

Time : Three hours

Maximum Marks : 70

Section – A

Answer any FIVE of the following questions. (5 × 4 = 20 Marks)

- 1) Person u/s 2(31) of Income Tax Act.
సెక్షన్ 2(31) ఆదాయ పన్ను చట్ట ప్రకారము వ్యక్తి.
- 2) Examples of partly agricultural and partly non agricultural.
పాక్షిక మరియు పాక్షికేతర వ్యవసాయ ఆదాయాలకు ఉదాహరణలిమ్ము.
- 3) Tax treatment of entertainment allowance.
. వినోద భత్యమునకు అంబడించిన పన్ను పరిశీలన.
- 4) Deductions u/s 24 of Income Tax Act.
సెక్షన్ 24 ఆదాయ పన్ను చట్ట ప్రకారము తగ్గింపులు.
- 5) Short term capital Assets.
స్వల్పకాల పెట్టుబడి ఆస్తులు.
- 6) Tax evasion.
పన్ను ఎగవేత.
- 7) Interest and dividend.
వడ్డీ మరియు డివిడెండ్.
- 8) Examples of capital receipts.
పెట్టుబడి వసూళ్లకు ఉదాహరణలిమ్ము.

Section – B

Answer the following questions. (5 x 10 = 50 Marks)

- 9) (a) State the examples of non agricultural incomes.

వ్యవసాయేతర ఆదాయాలకు ఉదాహరణలిమ్ము.

Or

- (b) Discuss the exempted incomes u/s 10 of Income Tax Act.

సెక్షన్ 10 ఆదాయ పన్ను చట్ట ప్రకారము మినహాయించబడిన ఆదాయాలను తెల్పుము..

- 10) (a) Explain the tax treatment of various kinds of provident fund.

వివిధ రకాలైన భవిష్య నిధులకు సంబంధించిన పన్ను వర్తింపు ప్రక్రియను వివరింపుము..

Or

- (b) Mr. Karthik is an employee in Indian Navy has furnished the following particulars of his income for the year ended 31st March, 2016. Compute taxable income for the assessment year 2017 – 2018.

	Rs.	
Basic salary	35,000	P.M.
Dearness pay	18,000	P.M.
Special allowance	4,000	P.M.
Gift in cash	10,000	
Entertainment allowance	10,000	
Employers contribution to RPF	5,000	P.M.
Employees contribution to RPF	5,000	P.M.
Interest on RPF credited @ 10% amounting to	9,000	
LIP paid on his own life	26,000	
Medical Insurance premium	12,000	

శ్రీ కార్తిక్ ఇండియన్ నేవీ లో ఉద్యోగి. మార్చి 31, 2016 అంతమయ్యే సంవత్సరానికి దిగువ వివరముల నుండి 2017 – 2018 పన్ను నిర్ధారణకు అతని యొక్క ఆదాయమును లెక్కింపుము.

	రూ.
మూల జీతము నెలకు	35,000
కరువు భత్యము నెలకు	18,000
ప్రత్యేక అలవెన్సు నెలకు	4,000
బహుమతి నగదు	10,000
వినోద భత్యము	10,000
గుర్తింపు పొందిన భవిష్య నిధికి యజమాని చెలించిన మొత్తము	5,000
గుర్తింపు పొందిన భవిష్య నిధికి ఉద్యోగి చెలించిన మొత్తము	5,000
గుర్తింపు పొందిన భవిష్య నిధికి 10% వడ్డీ చొప్పున జమ అయిన వడ్డీ	9,000
ఉద్యోగి చెలించిన జీవిత భీమా ప్రీమియము	26,000
వైద్య జీవిత భీమా ప్రీమియము చెలించిన మొత్తము	12,000

11) (a) Explain about the procedure for computation of Income from Business.

వ్యాపారం నుండి వచ్చే ఆదాయం కంప్యూట్ చేయు విధానాన్ని వివరించండి.

Or

(b) Mr. Avinash is the owner of a house property situated in Vijayawada. The following particulars are furnished for the assessment Year 2015 – 2016. Compute the taxable income.

	Rs.	
Fair rental value	50,000	P.M.
Standard rental value	52,500	P.M.
Municipal value	52,000	P.M.
Actual rental value	50,000	P.M.
Municipal Taxes	8%	
Municipal Taxes paid by owners	60%	
Interest on loan taken for purchase of a car	40,000	
Fire Insurance premium	3,750	

శ్రీ అవినాష్ విజయవాడలో నున్న గృహస్థి యజమాని. 2015 – 2016 నిర్ధారణ సంవత్సరమును దిగువ వివరముల నుండి ఆటను పన్ను చెల్లించవలసిన గృహస్థి ఆదాయమును లెక్కింపుము.

	రూ.
యుక్తమైన అద్దె విలువ నెలకు	50,000
ప్రామాణిక అద్దె నెలకు	52,500
మున్సిపల్ అద్దె నెలకు	52,000
వాస్తవ అద్దె నెలకు	50,000
మున్సిపల్ పన్ను	8%
యజమాని చెలించిన మున్సిపల్ పన్ను	60%
కారు కొనుగోలు నిమిత్తం పొందిన ఋణం పై వడ్డీ	40,000
అగ్ని భీమా ప్రీమియం	3,750

12) (a) What are the taxable incomes under the head income from other sources?

ఇతరత్రా ఆదాయ శీర్షిక క్రింద పన్ను చెల్లించవలసిన ఆదాయాలు ఏమిటి?

Or

(b) From the following information, calculate taxable income of Vaishnavi for the year ended 31st March, 2016.

	Rs.
Dividend received from Indian company	22,000
Examinership remuneration from the university	12,000
Gift received from the cousin of his father	50,000
Interest on bank deposits	14,000
Interest on government securities	24,000
Income from agricultural land in Bangladesh	1,20,000
Collection charges for dividend	5,000
Royalty from books and articles received	2,60,000

31 మార్చి, 2016 న వైష్ణవి దిగువ ఇచ్చిన సమాచారం నుండి ఆమె పన్ను చెల్లించవలసిన మొత్తము ఆదాయము లెక్కింపుము.

	రూ.
ఇండియన్ కంపెనీ నుండి పొందిన డివిడెండ్	22,000
విశ్వవిద్యాలయాల నుండి పొందిన పర్యవేక్షణ పారితోషికము	12,000
ఆసెసీ ఆమె తండ్రి యొక్క కజిన్ నుండి పొందిన బహుమతి	50,000
బ్యాంకు డిపాజిట్ల పై వడ్డీ	14,000
గవర్నమెంట్ సెక్యూరిటీల పై వడ్డీ	24,000
బంగ్లా దేశ్ లో నున్న వ్యవసాయ భూమి నుండి మొత్తము	1,20,000
డివిడెండ్ వసులు నిమిత్తము ఖర్చు	5,000
పుస్తకాలూ మరియు ఆర్టికల్స్ ద్వారా పొందిన రాయల్టీ	2,60,000

13) (a) Explain the deductions claimed u/s 80c of Income Tax Act.

సెక్షన్ 80c ఆదాయ పన్ను చట్ట ప్రకారము తగ్గింపులు గూర్చి వ్రాయుము.

Or

(b) Explain the qualifying deductions under section 80G of Income Tax Act towards donations.

సెక్షన్ 80G ఆదాయ పన్ను చట్ట ప్రకారము విరాళములు వాటి తగ్గింపు వివరములను తెలుపుము.

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Lesson – 1

INTRODUCTION TO INCOME TAX

Objectives :

The students will be able to

- understand the history of taxation system in the India.
- know the various components of the Income Tax Law
- determine the scope of total income of various persons.

Structure of the lesson:

- 1.1 Introduction
- 1.2 Types of Taxes
- 1.3 Definitions of Income Tax
- 1.4 Income – U/S-2(24)
- 1.5 Heads of Income
- 1.6 Gross Total Income (GTI)
- 1.7 Total Income (Sec.5)
- 1.8 Summary
- 1.9 Key Words
- 1.10 Self Assessment Questions
- 1.11 Suggested Readings

1.1 INTRODUCTION :

In India, income tax was introduced for the first time in 1860 by Sir James Wilson in order to meet the losses sustained by the Government on account of the Military Mutiny of 1857. Thereafter several amendments were made in it from time to time. After implementation of this Act, people became aware of the actual meaning of Income Tax. This act was in force for first five years. After this, in 1865, second Act came into force.

The Income Tax Law comprises The Income Tax Act 1961, Income Tax Rules 1962, Notifications and Circulars issued by Central Board of Direct Taxes (CBDT), Annual Finance Acts and Judicial pronouncements by Supreme Court and High Courts. The word 'Tax' originated from the 'Taxation.' which mean 'Estimate.' Hence, 'Income Tax' mean 'Income Estimate,' which helps the government to know the actual economic strength of a person. It helps the Government to know the distribution of money among country's people. Income Tax has been in force in

different forms since years. If we go through the history of India, we get relevant information regarding the taxation system of India. In ancient history, it is mentioned about such system which was imposed on the income, expenditure and other subject. Even information of the same is given in Manu Smriti and Arthasatra which confirms its existence at that time.

The taxation is the primary source of revenue to the Government for incurring such public welfare expenditure. In other words, Government is taking taxes from public through its one hand and through another hand; it incurs welfare expenditure for public at large. However, one enjoys handing over his/hard-earned money to the government to pay taxes. Thus, taxes are compulsory or enforced contribution to the Government revenue by public. Government may levy taxes on income, business profits or wealth or add it to the cost of some goods, services, and transactions.

1.2 TYPES OF TAXES :

Typically, the tax structure includes Direct tax and Indirect taxes.

A. Direct Tax : The definition of direct tax is hidden in its name which implies that this tax is paid directly to the government by the taxpayer. The general examples of this type of tax in India are Income Tax and Wealth Tax. From the government's perspective, estimating tax earnings from direct taxes is relatively easy as it bears a direct correlation to the income or wealth of the registered taxpayers. These are taxes that are levied on an individual and are directly payable to the Government. The Central Board of Direct Taxes (CBDT) is responsible for the governance of this tax.

Some important Direct taxes include :

- Income tax
- Wealth tax
- Gift tax
- Capital Gains tax
- Securities Transaction tax
- Corporate tax

Among these taxes, income tax is the most common tax levied on individuals. This tax is imposed on the income earned within a financial year. The tax rate is determined according to the applicable tax slab. Individuals include Hindu Undivided Family (HUF), company, firm, co-operative societies and trusts.

B. Indirect Taxes : Indirect taxes are charges levied indirectly on the public. These are mostly charged through goods and services. The seller takes these taxes in the prices, which are then collected by the concerned Government bodies.

Some important Indirect taxes include:

- Sales tax
- Goods and Services tax
- Value Added Tax (VAT)
- Customs duty
- Toll tax
- Octroi duty

In India, the central government introduced the Good and Services Tax (GST) in 2017, to incorporate a few taxes in one blanket. Some of the taxes replaced by GST are :

- Sales tax
- Service tax
- Octroi
- Central Excise duty
- Entertainment tax
- Purchase tax

GST is a multi-stage location-based tax, which is charged on each stage of the supply chain from the purchase of raw material, till the sale of finished product and then to the end consumer. Typically, wherever there are value addition and transfer of ownership in the supply, GST will be applicable.

GST is collected by the Government of the destination, where the final purchase takes place. GST has three components :

- Central Goods and Services Tax (CGST), where the central Government collects the charge on the supply of goods and services within the state
- State Goods and Services Tax (SGST), or UTGST for Union Territories, where the state Government/Union Territory collects taxes on the supply of goods and services within the state
- Integrated Goods and Services Tax (IGST), where the central Government collects taxes for the sale of goods and services beyond state borders.

1.3 DEFINITIONS OF INCOME TAX :

- a) Assessment Year - U/S-2(9) :** Financial Year starts from 1st April and end on 31st March. Assessment year is the year immediately following the financial year where in the income of the Financial Year is assessed.

For example : During the assessment year 2022-23, tax shall be paid for the previous year 2021-22.

- b) Previous Year - U/S-3:** “Previous Year” means the financial year immediately preceding the Assessment Year. In other words, the year in which income is earned is known as previous year.

For example : For the income accrued in FY 2021-22 will be taxed in assessment year 2022-23. So, Financial Year is the previous year while assessment year is the current year. Income earned in the previous year is evaluated and computed; tax on the income earned is paid in the current year or assessment year.

- c) Person-U/S-2(31) :** The term ‘Person’ as defined under the Income-tax covers in its ambit natural as well as artificial persons. For the purpose of charging Income-tax, the term ‘Person’ includes Individual, Hindu Undivided Families (HUF), Association of Persons (AOP), Body of Individuals (BOI), Firms, LLPs, Companies, Local authority and any artificial juridical person not covered under any of the above. Thus, from the definition of the term, person “ It can be observed that, apart from a natural person, i.e., an individual, any sort of artificial entity will also be liable to pay income-tax.

- d) Assesses- U/S-2(7) :** The term “Assessee” is considered as one who is supposed to pay tax under income tax. However, it is advisable to understand complete meaning of the term as envisaged under the Income Tax Act.

(i) Normal Assesses : Any person against whom proceedings under Income Tax Act are going on, irrespective of the fact whether any tax or other amount is payable by him or not;

- any person who has sustained loss and filed return of loss u/s 139(3),
- any person by whom some amount of interest, tax or penalty is payable under this Act ,
- Any person who is entitled to refund of tax under this Act.

(ii) Representative Assessee : A person may not be liable only for his own income or loss but he may also be liable for the income or loss of other persons.

Example : Agent of a non-resident, Guardian of minor or lunatic etc. In such cases, the person responsible for the assessment of income of such person is called representative assesses. Such person is deemed to be an assessee.

(iii) Deemed Assessee : In case of a deceased person who dies after writing his will the executors of the property of deceased are deemed as assessee. In case a person dies in the state (without writing his will) his eldest son or other legal heirs are deemed as assessee. In case of a minor, lunatic or idiot having

income taxable under Income tax Act, their guardian is deemed as assessee. In case of a non-resident having income in India, any person acting on his behalf is deemed as assessee.

(iv) Assessee-in-default : In-default a person is deemed to be an assessee-in-default if he fails to fulfill his statutory obligations. In case of an employer paying salary or a person who is paying interest, it is their duty to deduct tax at source and deposit the amount of tax so collected in Government treasury. If he fails to deduct tax at source or deducts tax but does not deposit it in the treasury, he is known as assessee-in-default.

1.4 INCOME – U/S-2(24) :

This term has not been defined in the Income tax Act. It includes the following :

- i) Profits and gains.
- ii) Dividend.
- iii) 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.
- iv) The value of any perquisite or profit in lieu of salary.
- v) Any special allowance or benefit, other than perquisite specifically granted to the assessee to meet expenses wholly, necessarily and exclusively for the performance of the duties of an office or employment of profit.
- vi) 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.
- vii) 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.
- viii) Any sum chargeable to income-tax under clauses (ii) and (iii) of section 28 or section 41 or section 59.
- ix) Any capital gains chargeable under section 45;
- x) The profits and gains of any business of insurance carried on by a mutual insurance company or by a co-operative society, computed in

accordance with section 44 or any surplus taken to be such profits and gains by virtue of provisions contained in the First Schedule;

- xi) Any winning 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.
- xii) Any sum received by the assessee from his employees as contributions to any provident fund or superannuation fund or any fund set up under the provisions of the Employees State Insurance Act.
- xiii) Any sum received under a Keyman insurance policy including the sum allocated by way of bonus on such policy.
- xiv) Any consideration received for issue of shares as exceeds the fair market value of the shares.
- xv) Any assistance in the form of a subsidy or grant or cash incentive or duty drawback or waiver or concession or reimbursement by the Central Government or a State Government or any authority or body or agency in cash or kind to the assessee other than 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 clause (1) of section 43.

1.5 HEADS OF INCOME :

The section 14 of Income Tax Act classifies all incomes under the following heads :

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

1) Income from Salaries : An income is taxable under salary head if there is a relationship of employer and employee. This means there should be a relationship between the payer and the payee. If the relationship does not exist or cannot be proved, then the income will not be deemed to be income from salary.

2) Income from House Property : The rental income earned from the house property is taxable under the Income from House Property. The income calculated is levied on the expected rent, if the property is not rented out. This would be the rent that would have been received from the property. Income from House Property is the only income that is taxed on a notional basis. Tax

is not only levied on the income from house property but income from commercial property and other forms of property. Various deductions such as tax deduction on a home loan interest are allowed under this income head.

- 3) Income From Business or Profession :** Any income that is earned from a trade/manufacture/commerce/profession shall be taxable under this head.
- 4) Income from Capital Gains :** Any profit or gain earned under a transfer of an asset in the effective financial year shall be chargeable under the head of Income of Capital Gains and shall be deemed to be the income of the financial year in which the transfer took place unless the gain is exempt under Section 54, 54B, 54D, 54EC, 54ED, 54F, 54G or 54GA.
- 5) Income from Other Sources :** Any income that does not come under the above 4 heads of income shall be chargeable under this head. The incomes computed under income from other sources are:
 - a) Interest on bank deposits and securities.
 - b) Dividends.
 - c) Income from sub-letting a house property by a tenant.
 - d) Insurance commission.
 - e) Income from royalty and more.

1.6 GROSS TOTAL INCOME (GTI) :

Gross Total Income is the aggregate of the incomes computed under various heads of income according to the provisions of the Income Tax Act before making any deduction u/s 80C to 80U.

Section 14 deals with the Gross Total Income and it includes :

- Income from Salaries;
- Income from House property;
- Income from Business or profession;
- Income from Capital Gains;
- Income from Other sources.

1.7 TOTAL INCOME (U/S-5) :

- Total income of an assessee is Gross Total Income after making deductions U/S80C to 80U.
- Total income means the total income referred to in section 5 and computed in the manner laid down in the Income Tax Act. Under Sec.5 different incomes of an assessee are included in his total income on the

basis of his residential status. It will be determined after making deductions under section 80C to 80U from gross total income.

Computation of Total Income :

Particulars	Amount	Amount
Income from Salaries		xxx
Income from House Property.		xxx
Income from Business/Profession.		xxx
Income from Capital Gains.		xxx
Income from Other Sources.		xxx
Gross Total Income		xxx
Less : Deductions under section 80		xxx
Total Income		xxx

Casual Income :

An income becomes casual income, if it contains the following features:

- It is unanticipated,
- It is non-recurring in nature,
- It arises from an unknown source,
- No specific efforts were put into earn such income.

For example :

- (i) Winning from lottery.
- (ii) Income from cross word puzzles and card games.
- (iii) Tips given to taxi drivers.
- (iv) Prize awarded for coin or stamp collection.

Tax treatment : Casual incomes are fully taxable under the head income from other sources.

- a) Maximum amount of casual income up to Rs. 5000 and Rs 2500 in case of horse race is exempted from income tax.
- b) Expense incurred to earn such income is not allowed as deduction.
- c) The benefit of basic exemption limits i.e. RS. 250000 are not allowed.

- d) In other words, if you earn Rs. 50,000 from casual income which is the total income in a F.Y then also tax will be deducted irrespective of basic exemption limit.
- e) Tax on casual income is deducted at flat rate of 30% for all assesses u/s 115BB.
- f) Losses cannot be set-off against casual income. Even casual losses cannot be set-off against casual income.

Tax Planning : It is a way to reduce tax liability by taking full advantages provided by the Act through various exemptions, deductions, rebates & relief. In other words, it is a way to reduce tax liability by applying script & moral of law. It is the scientific planning so as to attract minimum tax liability or postponement of tax liability for the subsequent period by availing various incentives, concessions, allowance, rebates and relief provided in the Act.

Tax Evasion : It is the illegal way to reduce tax liability by deliberately suppressing income or sale or by increasing expenses, etc., which results in reduction of total income of the assessee. Tax evasion is illegal, both in script & moral. It is the cancer of modern society and work as a clog in the development of the nation.

Tax Avoidance : It is an exercise by which the assessee legally takes advantages of loopholes in the Act. Tax avoidance is a practice of bending the law without breaking it. It is away to reduce tax liability by applying script of law only. Most of the amendments are aimed to curb such loopholes. There are two thoughts about tax avoidance– As per first thought it is legal. Such thought is also supported by various judgments of the Supreme Court; some of them are as follows–CWT Vs. Arvind Narotham (1988)

“It is true that tax avoidance in an underdeveloped or developing economy should not be encouraged on practical as well as ideological grounds. One would wish ...that one could get the enthusiasm...That taxes are the price of civilization and one would like to pay that price to buy civilization. But the question which many ordinary taxpayers very often, in a country of shortages with ostentatious consumption and deprivation for the large masses, ask is, does he with taxes buy civilization or does he facilitate the waste and ostentation of the few. Unless ostentation and waste in Government spending are avoided or eschewed, no amount of moral sermons would change people’s attitude to tax avoidance.”

As per second thought it is not a legal way to reduce tax burden and it should be prohibited – McDowell & Co. Ltd. Vs .Commercial Tax Officer (1985)

Supreme Court observed-

“We think time has come for us to depart from Westminster principle....tax planning may be legitimate provided it is within the framework of law. Colourable

devices cannot be part of tax planning and it is wrong to encourage or entertain the belief that it is honourable to avoid the payment of tax by resorting to dubious methods. It is the obligation of every citizen to pay the honestly without resorting to subterfuges.”

Income Tax Slab :

Tax Slab	Rates
Up to Rs. 3,00,000	NIL
Rs. 300,000 to Rs. 6,00,000	5% on income which exceeds Rs 3,00,000
Rs. 6,00,000 to Rs. 900,000	Rs 15,000 + 10% on income more than Rs 6,00,000
Rs. 9,00,000 to Rs. 12,00,000	Rs 45,000 + 15% on income more than Rs 9,00,000
Rs. 12,00,000 to Rs. 1500,000	Rs 90,000 + 20% on income more than Rs 12,00,000
Above Rs. 15,00,000	Rs 150,000 + 30% on income more than Rs 15,00,000

Income Tax Slab for People between 60 to 80 Years

Tax Slabs	Rates
Rs. 3 lakhs	NIL
Rs. 3 lakhs - Rs. 5 lakhs	5%
Rs. 5 lakhs - Rs. 10 lakhs	20%
Rs. 10 lakhs and more	30%

Income Tax Slab for People More than 80 Years.

Below mentioned is the Senior citizen tax slab in detail -

Tax Slabs	Rates
Rs. 0 - Rs. 5 lakhs	NIL
Rs. 5 lakhs - Rs. 10 lakhs	20%
Above Rs. 10 lakhs	30%

Tax Slabs for Domestic Companies :

Particulars	Existing or Old Regime Tax Rates	New Regime Tax Rates
Company opts for section 115BAB (not covered in section 115BA and 115BAA) & is registered on/after October 1, 2019 and has started manufacturing on/before 31st March 2023	-	15%
Company opts for Section 115BAA , where the total income of a company has been calculated without claiming specified deductions, exemptions, incentives, and additional depreciation	-	22%
Company opts for section 115BA registered on/after March 1, 2016, and is in the manufacture of any article or thing and does not claim a deduction as specified in the section	-	25%
Turnover/gross receipt of the company is less than Rs. 400 crores in the previous year	25%	25%
Other Domestic Company	30%	30%

- Surcharge applicable for companies-
 - 7% of Income tax where total income is more than Rs 1 crore
 - 12% of Income tax where total income is more than Rs.10 crores
 - 10% of income tax where domestic company opted Section 115BAA and 115BAB
- Additional Health & Education Cess Rate - 4%

Income Tax Rate for Partnership Firm or LLP as Per Old/New Regime

A partnership firm or an LLP is taxable at 30%

Note : A Surcharge of 12% is levied on incomes above Rs 1 crore.

Health and Education Cess Rate - 4 %

Income Tax Slab Rate for New Tax Regime

The HUF and Individual tax slab applicable are :

Slab	New Tax Regime (Before Budget 2023 - until 31 March 2023)	New Tax Regime (After Budget 2023 - From 01 April 2023)
Rs. 0 to Rs. 2,50,000	NIL	NIL
Rs. 2,50,000 to Rs. 3,00,000	5%	NIL
Rs. 3,00,000 to Rs. 5,00,000	5%	5%
Rs. 5,00,000 to Rs. 6,00,000	10%	5%
Rs. 6,00,000 to Rs. 7,50,000	10%	10%
Rs. 7,50,000 to Rs. 9,00,000	15%	10%
Rs. 9,00,000 to Rs. 10,00,000	15%	15%
Rs. 10,00,000 to Rs. 12,00,000	20%	15%
Rs. 12,00,000 to Rs. 12,50,000	20%	20%
Rs. 12,50,000 to Rs. 15,00,000	25%	20%
More than Rs. 15,00,000	30%	30%

Agricultural Income : Sec. 2(1A) Agriculture income is exempt under the Indian Income Tax Act. This means that income earned from agricultural operations is not taxed. However while computing tax on non-agricultural income; agricultural income is also taken into consideration. Agriculture income is computed same as business income. Losses from agricultural operations could be carried forward and set off with agricultural income of next eight assessment years.

Agricultural Income means :

As per Income Tax Act, income earned from any of the under given three sources meant Agricultural Income;

- i. Any rent received from land which is used for agricultural purpose. Any income derived from such land by agricultural operations including processing of agricultural produce, raised or received as rent in kind so as to render it fit for the market, or sale of such produce.
- ii. Income attributable to a farm house subject to the condition that building is situated on or in the immediate vicinity of the land and is used as a dwelling house, store house etc. Now income earned from carrying nursery operations is also considered as agricultural income and hence exempt from income tax.

In order to consider an income as agricultural income certain points have to be kept in mind :

- a. There must be a land and it must be situated in India.
- b. The land is being used for agricultural operations.
- c. Agricultural operation means that efforts have been induced for the crop to sprout out of the land.
- d. If any rent is being received from the land then in order to assess that rental income as agricultural income there must be agricultural activities on the land.
- e. In order to assess income of farm house as agricultural income the farm house building must be situated on the land itself only and is used as a store house / dwelling house.

Certain income which is treated as Agriculture Income;

- i. Income from sale of replanted trees.
- ii. Rent received for agricultural land.
- iii. Income from growing flowers and creepers.
- iv. Share of profit of a partner from a firm engaged in agricultural operations.
- v. Interest on capital received by a partner from a firm engaged in agricultural operations.
- vi. Income derived from sale of seeds.

Certain income which is not treated as Agricultural Income :

- a) Income from poultry farming.
- b) Income from bee hiving.
- c) Income from sale of spontaneously grown trees.
- d) Income from dairy farming.

- e) Purchase of standing crop.
- f) Dividend paid by a company out of its agriculture income.
- g) Income of salt produced by flooding the land with sea water.
- h) Royalty income from mines.
- i) Income from butter and cheese making.
- j) Receipts from TV serial shooting in farm house are not agriculture income.

1.8 SUMMARY :

Financial year starts from 1st April and ends on 31st March (wherein there is income pertaining to the whole year or part of the year). Assessment year is the year immediately following the financial year wherein the income of the F.Y. is assessed. Previous Year” means the financial year immediately preceding the assessment year. In other words, the year in which income is earned is known as previous year and the next year in which this income is taxable is known as assessment year.

For the purpose of charging Income-tax, the term “person” includes Individual, Hindu Undivided Families [HUFs], Association of Persons [AOPs], Body of individuals [BOIs], Firms, LLPs, Companies, Local authority and any artificial juridical person not covered under any of the above.

The term “income” has not been defined in the Income Tax Act.

It includes the following :

- a. Profits and gains;
- b. Dividend;
- c. 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, etc.

1.9 KEY WORDS :

1. Agricultural Income :

Agriculture income is exempt under the Indian Income Tax Act. This means that income earned from agricultural operations is not taxed.

2. Tax Planning :

It is a way to reduce tax liability by taking full advantages provided by the Act through various exemptions, deductions, rebates & relief. In other words, it is a way to reduce tax liability by applying script & moral of law.

3. Tax Evasion :

It is the illegal way to reduce tax liability by deliberately suppressing

income or sale or by increasing expenses, etc., which results in reduction of total income of the assessee. Tax evasion is illegal, both in script & moral. It is the cancer of modern society and work as a clog in the development of the nation.

4. Tax Avoidance :

It is an exercise by which the assessee legally takes advantages of loopholes in the Act. Tax avoidance is a practice of bending the law without breaking it. It is away to reduce tax liability by applying script of law only. Most of the amendments are aimed to curb such loopholes.

1.10 SELF ASSESSMENT QUESTIONS :

1. Who is an Assessee?
2. What is previous year and assessment year?
3. Who is Person?
4. What is Agricultural Income?
5. Write a short note on Income Tax Act 1961.
6. What is Tax?
7. Why are taxes levied?
8. Under How Many Heads the Income of a Taxpayer Is Classified?
9. What Is Surcharge and How It Is Computed?
10. As an agriculturist, am I required to maintain any proof of earning and expenditure incurred?
11. I win a lottery or prize money in a competition. Am I required to pay taxes on it?

1.12 SUGGESTED READINGS :

1. R. K. Jain, Nikhil Gupta, Manoj Kumar Agrawal, Sanjeev S. Thakur, '*Practical Problems in Income Tax*', Scorer Guru Publications, Agra, 2023.
2. Dr. H. C. Mehrotra, Dr. S. P. Goyal, '*Problems and Solutions in Income Tax - Assessment Year 2022-23*', Sahitya Bhawan Publications, Agra, 2022.
3. Dr. H.C. Mehrotra, Dr. S.P. Goyal, '*Corporate Tax Planning & Management A.Y 2020-21 & 2021-22*', Sahitya Bhawan Publications, Agra, 2020.

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Lesson – 2

RESIDENTIAL STATUS AND EXEMPTED INCOMES

Objectives :

The students will be able to

- understand the residential status of an assessee and various conditions to be followed in determination of residential status.
- know about various incomes exempted under Income Tax Act, 1961.
- determine the scope of total income and tax liability of various persons.

Structure of the lesson :

- 2.1 Meaning and Scope of Total Income (Section 5)
- 2.2 Residential Status and Tax Liability (Section 6)
- 2.3 Residential Status of Individuals
- 2.4 Additional Conditions for an Individual to Be Resident and Ordinary Resident
- 2.5 Resident and Not Ordinary Resident (RNOR)
- 2.6 Residential Status of Hindu Undivided Families
- 2.7 Income Deemed to Accrue or Arise In India
- 2.8 Agricultural Income [Section 10(1)]
- 2.9 Summary
- 2.10 Key Words
- 2.11 Self Assessment Questions
- 2.12 Suggested Readings

2.1 MEANING AND SCOPE OF TOTAL INCOME (SECTION 5) :

The scope of total income and consequently the liability to income tax depends upon the following facts :

- a. Whether the income accrues or is received in India or outside,
- b. The exact place and point of time at which the accrual or receipt of income takes place, and
- c. The residential status of the assessee. Scope of Total income has been defined on the basis of Residential status 1. Resident and Ordinarily Resident Assessee According to Sub-section.

- (1) Of Section 5 of the Act the total income of a resident and ordinarily resident assessee would consist of :
1. Income received or deemed to be received in India during the accounting year by or on behalf of such person;
 2. Income which accrues or arises or is deemed to accrue or arise to him in India during the accounting year;
 3. Income which accrues or arises to him outside India during the accounting year. It is important to note that under clause (iii) only income accruing or arising outside India is included. Income deemed to accrue or arise outside India is not includible in the total taxable income.
- (2) Resident but Not Ordinarily Resident in India Proviso to section (1) of section 5 provides that the total income in case of resident but not ordinarily resident in India would consist of :
- i. income received or deemed to be received in India during the accounting year by or on behalf of such person;
 - ii. income which accrues or arises or is deemed to accrue or arise to him in India during the accounting year;
 - iii. income which accrues or arises to him outside India during the previous year if it is derived from a business controlled in or a profession set up in India.
- (3) **Non-Resident** Sub-section (2) of Section 5 provides that the total income of a non-resident would comprise of :
- i. Income received or deemed to be received in India in the accounting year by or on behalf of such person;
 - ii. Income which accrues or arises or is deemed to accrue or arise to him in India during the previous year.

2.2 RESIDENTIAL STATUS AND TAX LIABILITY (SECTION 6) :

According to the residential status, the assessee can either be; Resident in India, or Non-resident in India.

However, a resident individual and a resident HUF can further be classified as :

Resident and ordinarily resident in India (ROR) or Resident but not ordinarily resident in India (RNOR). It must be noted that only an individual or a HUF can be resident, not ordinarily resident or non-resident in India.

All other assesses can be either resident or non-resident in India but cannot be not ordinarily resident in the matter of their residential status for all purposes of income tax. Section 6 of the Income-tax Act prescribes the conditions to be fulfilled by various taxpayers to determine their residential status.

2.3 RESIDENTIAL STATUS OF INDIVIDUALS :

An individual first needs to satisfy basics condition in order to become resident in India. If a resident individual satisfies additional conditions, he becomes resident and ordinarily resident (ROR), otherwise he is resident but not ordinarily resident (RNOR).

Basic Conditions for an Individual to be Resident : Under Section 6(1) of the Income-tax Act, an individual is said to be resident in India in any previous year if he:

- He has been in India for at least 182 days during the previous year; or,
- He has been in India for at least sixty days (60 days) during the previous year and for at least three hundred and sixty-five days (365 days) during the four years immediately preceding the previous year.

Exceptions to above conditions in the following two cases, second condition is not applicable, i.e., if condition (1) is satisfied then an individual is resident otherwise he will be non-resident :

- i. The individual is a citizen of India, who leaves India in any previous year as a member of the crew of an Indian ship, or for the purpose of employment outside India, or
- ii. The individual is a citizen of India or person of Indian origin engaged outside India (whether for rendering service outside or not) and who comes on a visit to India in the any previous year. Therefore, in the above two exceptional cases, only the basic condition 1 needs to be checked. If it is satisfied, then the individual is treated as a resident, otherwise he will be treated as non-resident.

NON-RESIDENT :

- If an individual does not satisfy any of the above two basic conditions then, he will be treated as non-resident.
- It must be noted that the fulfillment of any one of the above conditions 1 or will make an individual resident in India since both these conditions are alternative and not cumulative in their application.

2.4 ADDITIONAL CONDITIONS FOR AN INDIVIDUAL TO BE RESIDENT AND ORDINARY RESIDENT (ROR)

An individual may become a resident and ordinarily resident in India if he satisfies both the following conditions given u/s 6(1) besides satisfying any one of the above mentioned conditions :

1. He is a resident in at least any two out of the ten previous years immediately preceding the relevant previous year, and

2. He has been in India for 730 days or more during the seven previous years immediately preceding the relevant previous year.

2.5 RESIDENT AND NOT ORDINARY RESIDENT (RNOR) :

If a resident individual is not able to satisfy both the additional conditions, then he will be resident but not ordinary resident (RNOR).

2.5.1. Steps to solve Residential Status of an Individual :

Determine whether the person falls under exception to basic condition;

1. If yes, apply only first basic condition, if satisfied, then he will be resident otherwise non- resident. If the person does not fall under exception to basic condition, then apply both basic conditions. Individual becomes resident on satisfaction of any one condition.
2. Resident Individual will be called ROR if satisfies both the additional conditions, otherwise he will be called RNOR.

Important Points to be considered while determining Residential Status The residential status of the assessee should be determined for each year separately. This is because a person resident in one year may become non-resident or not ordinarily resident in another year and vice versa.

1. The residential status of an individual for tax purposes does not depend upon his citizenship, nationality and place of birth or domicile. This is because for tax purposes, an individual may be resident in more than one country in respect of the same year.
2. The period of stay required in each of the conditions need not necessarily be continuous nor is the purpose of stay is insignificant in determining the residential status.
3. It is not required that the stay should be at the usual place of residence, business or employment of the individual. The stay may be anywhere in India and for any length of time at each place.
4. India means territory of India, its territorial waters, continental shelf, Exclusive Economic Zone (up to 200 nautical miles) and airspace above its territory and territorial waters.
5. Where the exact arrival and departure time is not available then the day he comes to India and the day he leaves India is counted as stay in India.

Incidence of Tax

S. No.	Particulars	Resident	Not ordinarily Resident	Non-Resident
1.	Income received or deemed to be received in India, irrespective of the being accrued or earned outside India	Taxable	Taxable	Taxable
2.	Income accrued or earned or deemed to be accrued or earned in India, irrespective of the income being received in India or outside India.	Taxable	Taxable	Taxable
3.	Income received or accrued or earned outside India from business controlled from India. Irrespective of the income being remitted to India.	Taxable	Non Taxable	Non Taxable
4.	Income received or accrued or earned outside India from any other sources salary, house property, capital gain or income from other sources.	Taxable	Taxable	Non Taxable
5.	Income received or accrued or earned outside India from any other sources salary, house property, capital gain or income from other sources.	Taxable	Non Taxable	Non Taxable
6.	Income earned and received outside India during the preceding the previous year and remitted to India during the previous year.	Non Taxable	Non Taxable	Non Taxable

2.6 RESIDENTIAL STATUS OF HINDU UNDIVIDED FAMILIES :

An HUF can be a resident or non-resident. Similar to an individual, it can further be classified as a resident and ordinarily resident (ROR) or resident but not ordinarily resident (RNOR).

2.6.1 Basic Condition to be Resident/Non Resident :

A HUF is said to be resident in India within the meaning of Section 6(2) in any previous year, if during that year the control and management of its affairs is situated wholly or partly in India. If the control and management of its affairs is

situated wholly outside India during the relevant previous year, it is considered non-resident. Meaning of place of control and management the control and management is situated at that place where policy decisions are taken not the places where from the business is carried on. Policy decisions should be related with finance, marketing, production, advertising, personnel etc. It does not mean day to day operations of the concern / assessee. Control and Management of HUF lies with Karta or its Manager.

2.6.2 Additional Condition for an HUF to be Resident and Ordinary Resident (ROR) :

If the manager or Karta of A Resident HUF satisfies both the following additional conditions (as applicable in case of Individual) then Resident HUF will be ROR, otherwise it will be RNOR, i.e., if the

1. Karta of Resident HUF is resident in at least 2 previous years out of 10 previous year immediately preceding relevant previous year, and
2. Stay of Karta during 7 previous year immediately preceding relevant previous year is 730 days or more, then the HUF is an ROR, otherwise an RNOR.

2.6.3 Residential Status of Firms/AOP/Other Artificial Judicial Persons :

Firms, association of persons, local authorities and other artificial juridical persons can be either resident (ordinarily resident) or non-resident in India but they cannot be not ordinarily resident in India. These are said to be resident in India within the meaning of Section 6(2) in any previous year, if during that year the control and management of its affairs is situated wholly or partly in India. If the control and management of its affairs is situated wholly outside India during the relevant previous year, it is considered non-resident.

2.6.4 Residence for Companies :

All Indian companies within the meaning of Section 2(26) of the Act are always resident in India regardless of the place of control and management of its affairs. According to Section 6(3) a non-Indian company (foreign company) would be resident in India only if the whole of the control and management of its affairs throughout the relevant previous year are exercised from India. In other words, even if a negligible part of the control and management is exercised from outside India the company would be a non-resident for income-tax purposes.

2.6.5 Income Received :

Income received in India is taxable regardless of the assessee residential status therefore it has great significance.

- i. The receipt contemplated for this purpose refers to the first receipt of the amount in question as the income of the assessee. For instance, if A receives his salary at Delhi and sends the same to his father, the salary income of A is a receipt for tax purposes only in the hands of A; his father cannot also be said to have received income when he receives a part of the income of A. In the

hands of A's father it is only a receipt of a sum of money but not a receipt of income.

- ii. The taxable income of an assessee shall be calculated according to the method of accounting (cash system or mercantile system of accounting) that the assessee follows.
- iii. While considering the receipt of income for tax purposes both the place and the date of its receipt must be taken into account. The income in question should be not only received during the relevant previous year but must also be received in India in order to constitute the basis of taxation.
- iv. Receipt by some other person on behalf of the assessee should be treated as receipt by the assessee for being taxed in his hands.
- v. The question of taxability of a particular income received by the assessee depends upon the nature of income. For instance, income from salaries and interest on securities would attract liability to tax immediately when it falls due to the assessee regardless of its actual receipt by or on behalf of the assessee.

2.6.6 Income Deemed to be Received :

In addition to the income actually received by the assessee or on his behalf, certain other incomes not actually received by the assessee and/or not received during the relevant previous year, are also included in his total income for income tax purposes. Such incomes are known as income deemed to be received. Some of the examples of such income are :

- All sums deducted by way of taxes at source (Section 198).
- Incomes of other persons which are included in the income of the assessee under Sections 60 to 64.
- The amount of unexplained or unrecorded investments (Section 69).
- The amount of unexplained or unrecorded moneys, etc. (Section 69A).
- The transferred balance in a Recognized Provident Fund to the extent provided in Rule 11(4) of Part A - Fourth Schedule [Section 7(ii)].
- Any dividend declared by a Company or distributed or paid by it within the meaning of Section 2(22) [Section 8(a)]

2.7 INCOME DEEMED TO ACCRUE OR ARISE IN INDIA :

According to section 9 of the Act, certain incomes are deemed to accrue or arise in India which is discussed below:

- (1) Income by virtue of business connection Income arising through or from business connection to any assessee is deemed to accrue or arise in India

where a business connection actually exists whether with or without a regular agency, branch or other type of commercial association. The expression business connection includes:

- i. the maintenance of a branch office, factory, agency, receivership, management or other establishment for the purchase or sale of goods or for transacting any other business;
 - ii. The erection of a factory where the raw products purchased locally are processed or converted into some form suitable for export outside India;
 - iii. Appointing an agent or agents in India for the systematic and regular purchase of raw materials or other commodities or for the sale of the non-residents goods, or for any other purpose;
 - iv. The formation of a close financial association between a resident and a non-resident company which may or may not be related to one another as a holding and subsidiary company;
 - v. The formation of a subsidiary company to sell or otherwise deal with the products of the non-resident parent company;
 - vi. The grant of a continuing license to a non-resident for the purpose of exploitation for profit of an asset belonging to the non-resident even though the transaction in question may be treated as an out and out sale by the parties concerned.
- (2) Income arising from any asset or property in India Income arising in a foreign country from any property situated in India would be deemed to accrue or arise in India. In this context, the term property refers to all tangible properties whether movable or immovable.
- (3) Capital asset Capital gains arising to an assessee from the transfer of a capital asset situated in India would be deemed to accrue or arise in India irrespective of the fact whether the capital asset in question represents a movable or immovable property or a tangible or intangible asset.
- (4) Income from salaries Income which is chargeable under the head Salaries is deemed to accrue or arise in India in all cases when earned in India. For this purpose income is said to be earned in India if the services are rendered in India. Income from salaries payable by the Government to a citizen of India outside India for his services rendered outside India, is deemed to accrue or arise in India even though the income is actually accruing outside India and is also received outside India.
- (5) Taxability of Interest payable in following cases will be deemed to accrue or arise in India and will be taxable in the hands of recipient irrespective of his residential status (i.e. ROR, RNOR or NR). Interest payable by :
- i. Government; or

- ii. A Resident in India, except where interest is payable in respect of moneys borrowed and used for the purpose of business or profession carried outside India or earning any income from any source outside India (i.e. Interest payable by a Resident for loan used in India for any purpose, whether for business or profession or otherwise);
 - iii. A Non-Resident in India provided interest is payable in respect of moneys borrowed and used for a business or profession carried on in India (i.e. Interest payable by a Non-Resident for loan used for only business or profession in India)
- (6) Taxability of Royalty payable in following cases will be deemed to accrue or arise in India and will be taxable in the hands of recipient irrespective of his residential status (i.e. ROR, RNOR or NR). Royalty payable by :
- i. Government; or
 - ii. A Resident in India except where it is payable in respect of any right/ information/ property used for the purpose of a business or profession carried on outside India or earning any income from any source outside India (i.e. Royalty payable by a Resident for right/information/property used for any purpose in India whether business or profession or for earning other incomes);
 - iii. A Non-Resident in India provided royalty is payable in respect of any right/ information/ property used for the purpose of the business or profession carried on in India or earning any income from any source in India (i.e. Royalty payable by a Non- Resident for right/information/property used for any purpose in India whether business or profession or for earning other incomes).
- (7) Taxability of Fees for Technical Services: Fees for technical services payable in following cases will be deemed to accrue or arise in India and will be taxable in the hands of recipient irrespective of his residential status (i.e. ROR, RNOR or NR). Fees for technical services payable by :
- i. Government; or
 - ii. A Resident in India except where services are utilized for the purpose of a business or profession carried on outside India or earning any income from any source outside India (i.e. Fees for technical services payable by a Resident for services utilized for any purpose in India whether business or profession or for earning other incomes)
 - iii. A Non-Resident in India provided fee is payable in respect of services for the purpose of a business or profession carried on in India or earning any income from any source in India (i.e. Fees for technical services payable by a Resident for services utilized for any purpose in India whether business or profession or for earning other incomes);

- (8) Taxability of Dividend paid by any Indian company outside India is deemed to accrue or arise in India and the income is consequently chargeable to income-tax irrespective of the fact whether the dividend is interim dividend or a final dividend and whether it is an actual dividend or a notional dividend.

EXEMPTED INCOMES :

For providing relief to the tax payers from payment of tax, income tax law provisions contains concept of exemption and deduction. Exempted income means the income which is not at all charged to any taxes, while calculating the Gross Total Income. Whereas deduction means the amount which needs to be included in the income first then it is allowed for deduction in full or in part on fulfillment of certain conditions.

Under Section 10, 10AA, 11, 12, 12A, 13 and 13A of the Income-tax Act, various items of income are totally exempt from income-tax. Therefore, these incomes shall not be included in the total income of an assessee, provided the assessee proves that a particular item of income is exempt and falls within a particular clause. The items of exemptions 'specified in Section 10, are explained as follows :

2.8 AGRICULTURAL INCOME [SECTION 10(1)] :

Agricultural income as defined in Section 2(1A) is exempt from income-tax in the case of all assesses. Agricultural income is defined under section 2(1A) of the Income-tax Act.

2.8.1 As per Section 2(1a), Agricultural Income Generally, Means :

- a. Any rent or revenue derived from land which is situated in India and is used for agricultural purposes.
- b. Any income derived from such land by agriculture operations including processing of agricultural produce so as to render it fit for the market or sale of such produce.
- c. Any income attributable to a farm house subject to satisfaction of certain conditions specified in this regard in section 2(1A).

2.8.2 Amount Received by a Member of the HUF [Section 10(2)] :

As per section 10(2), amount received out of family income, or in case of impartibly estate, amount received out of income of family estate by any member of such HUF is exempt from tax in the hands of the member, because that has been taxed in hand of H.U.F.

2.8.3 Share of Profit Received by a Partner from The Firm [Section 10(2a)] :

As per section 10(2A), share of profit received by a partner from a firm is exempt from tax in the hands of the partner. Further, share of profit received by a

partner of LLP from the LLP will be exempt from tax in the hands of such partner. This exemption is limited only to share of profit and does not apply to interest on capital and remuneration received by the partner from the firm/LLP.

2.8.4 Certain Interest to Non-Residents [Section 10(4)] :

As per section 10(4)(i), in the case of a non-resident any income by way of interest on certain notified securities or bonds (including income by way of premium on the redemption of such bonds) is exempt from tax.

As per section 10(4)(ii), in the case of an individual, any income by way of interest on money standing to his credit in a Non-Resident (External) Account in any bank in India in accordance with the Foreign Exchange Management Act, 1999, and the rules made there under is exempt from tax.

2.8.5 Interest on Notified Savings Certificates [Section 10(4b)] :

As per section 10(4B), in the case of an individual, being a citizen of India or a person of Indian origin, who is a non-resident, any income by way of interest on notified savings certificates (subscribed in convertible foreign exchange) issued before the 1st day of June, 2002 by the Central Government is exempt from tax.

2.8.6 Leave Travel concession [Section 10(5)] :

An employee (Indian as well as foreign citizens) can claim exemption under section 10(5) in respect of Leave Travel Concession. Exemption is available in respect of value of any travel concession or assistance received or due to the employee from his employer (including former employer) for himself and his family members in connection with his proceeding on leave to any place in India. Quantum of exemption will be as follows :

- i. Where journey is performed by air, amount of exemption will be lower of amount of economy class air fare of the National Carrier by the shortest route or actual amount spent.
- ii. Where place of origin of journey and destination are connected by rail and the journey is performed by any mode of transport other than by air, air-conditioned first class rail fare by the shortest route to the place of destination.
- iii. Where the place of origin and destination are not connected by rail and journey is performed by any mode of transport other than by air the exemption will be :
 - If recognized public transport exists, lower of first class or deluxe class fare by the shortest route or actual amount spent.
 - If no recognized public transport exists, lower of amount of air conditioned first class rail fare by the shortest route (considering as if journey is performed by rail) or actual amount spent.

2.8.7 Exemptions to an individual who is not a citizen of India [section 10(6)] :

Remuneration of Diplomats etc. [Section 10(6) (ii)] In case of an individual who is not a citizen of India, remuneration received by him as an official (by whatever name called) of an embassy, high Commission, legation, Commission, consulate or trade representative of a foreign State, or member of the staff of any of that official is exempt from tax, if corresponding Indian official in that foreign country enjoys a similar exemption. Salary of a foreign employee and non-resident member of crew [Section 10(6) (vi), (viii)] As per section 10(6)(vi), the remuneration received by a foreign national as an employee of a foreign enterprise for services rendered by him during his stay in India is exempt from tax, provided the following conditions are fulfilled—

- The foreign enterprise is not engaged in any trade or business in India;
- His stay in India does not exceed in the aggregate a period of 90 days in such year; such remuneration is not liable to be deducted from the income of the employer.

As per section 10(6)(viii), any salaries received by or due to a nonresident foreign national for services rendered in connection with his employment on a foreign ship where his total stay in India does not exceed in the aggregate a period of 90 days in the year is exempt from tax. Remuneration of a foreign trainee [Section 10(6) (xi)] As per section 10(6)(xi), the remuneration received by a foreign trainee as an employee of foreign Government during his stay in India in connection with this training in any establishment or office of, or in any undertaking owned by,—

- i. the Government ; or
- ii. any company owned by the Central Government, or any State Government
- iii. any company which is a subsidiary of a company referred to in item (ii) ; or
- iv. any corporation established by or under a Central, State or Provincial Act ; or
- v. any co-operative society wholly financed by the Central Government, or any State Government.

Tax paid on behalf of foreign company deriving income by way of royalty or fees for technical services [Section 10(6A)] Tax paid by Central Government, State Government or an Indian concern on behalf of a foreign company deriving income by way of royalty or fees for technical services in pursuance of an agreement made after March 31, 1976 but before June 1, 2002 will be exempt from tax in the hands of such foreign company provided such agreement is in accordance with the industrial policy of the Indian Government or it is approved by the Central Government. Tax paid on behalf of foreign company or non-resident in respect of other income [Section 10(6B)] Tax paid by Central Government, State Government or an Indian concern on behalf of a foreign company or non-resident in respect of any income (not being salary, royalty or fees for technical services) will be exempt from tax in

the hands of such foreign company or non-resident if such income is received in pursuance of an agreement entered into before June 1, 2002 by the Central Government with the Government of a foreign State or international organization or any other related agreement approved by the Central Government.

2.8.8 Allowance/Perquisites to Government Employee outside India [Section 10(7)] :

As per section 10(7), any allowances or perquisites paid or allowed as such outside India by the Government to a citizen of India for rendering service outside India is exempt from tax.

2.8.9 Income of Foreign Government Employee Under Co- Operative Technical Assistance Programme [Section 10(8)] :

As per section 10(8), remuneration received directly or indirectly by an individual, from the foreign Government in connection with a cooperative technical assistance programme and projects in accordance with an agreement entered into by the Central Government and such foreign Government, is exempt from tax. Further, exemption is available in respect of any other income of such an individual which accrues or arises outside India and is not deemed to accrue or arise in India, provided such individual is required to pay income-tax/ social security tax to the foreign Government.

2.8.10 Death-cum-Retirement Gratuity received by Government Servants [Section 10(10) (i)] :

The amount of any death-cum-retirement gratuity received by Government employee (i.e., Central Government or State Government or local authority) is wholly exempt from tax under Section 10(10)(i) of the Act.

2.8.11 Gratuity Received by a Non-Government Employee Covered by Payment of Gratuity Act, 1972 [Section 10(10) (II)] :

As per section 10(10)(ii), exemption in respect of gratuity in case of employees covered by the Payment of Gratuity Act, 1972 will be lower of following:

15 days' salary \times years of service.

Maximum amount specified, i.e., Rs. 20,00,000.

Gratuity actually received.

Note:

Instead of 15 days 'salary, only 7 days salary will be taken into consideration in case of employees of seasonal establishment.

- a) 15 days' salary = Salary last drawn \times 15/26
- b) Salary for this purpose will include basic salary and dearness allowance only. Items other than basic salary and dearness allowance are not to be considered.

- c) In case of piece rated employee, 15 days' salary will be computed on the basis of average of total wages (excluding overtime wages) received for a period of three months immediately preceding the termination of his service.
- d) Part of the year, in excess of 6 months, shall be taken as one full year.

2.8.12 Gratuity received by a Non-government employee not covered by payment of Gratuity act, 1972 [Section 10(10)(iii)] :

As per section 10(10)(iii), exemption in respect of gratuity in case of employees not covered by the Payment of Gratuity Act, 1972 will be lower of following :

Half month's salary for each completed year of service, i.e., [Average monthly salary $\times \frac{1}{2}$] \times Completed years of service.

Maximum limit Rs. 20, 00,000.

Gratuity actually received.

Note:

- Average monthly salary is to be computed on the basis of average of salary for 10 months immediately preceding the month of retirement.
- Salary for this purpose will include basic salary, dearness allowance, if the terms of service so provide and commission based on fixed percentage of turnover achieved by the employee.
- While computing years of service, any fraction of a year is to be ignored.

2.8.13 Pension [Section 10(10A)] :

As per section 10(10A), any commuted pension, i.e., accumulated pension in lieu of monthly pension received by a Government employee is fully exempt from tax. Exemption is available only in respect of commuted pension and not in respect of un-commuted, i.e., monthly pension.

Exemption in respect of commuted pension in case of a non-Government employee will be as follows :

- If the employee receives gratuity, one third of full value of commuted pension will be exempt from tax under section 10(10A).
- If the employee does not receive gratuity, one half of full value of commuted pension will be exempt from tax under section 10(10A).

2.8.14 Leave Salary [Section 10(10AA)] :

As per section 10(10AA), leave encashment by a Government employee at the time of retirement (whether on superannuation or otherwise) is exempt from tax.

In the hands of non-Government employee exemption will be least of the following :

- Period of earned leave standing to the credit in the employee's account at the time of retirement \times Average monthly salary
- Average monthly salary \times 10 (i.e., 10 months' average salary).
- Maximum amount as specified by the Government, i.e., Rs. 3,00,000.
- Leave encashment actually received at the time of retirement.

Leave credit to the account of the employee at the time of retirement should be restricted to 30 days per year of service if leave entitlement as per service rules exceeds 30 days per year of actual service. Salary for the above purpose means average salary drawn in the past ten months immediately preceding the retirement (i.e., preceding the day of retirement) and will include basic salary, dearness allowance (if considered for computing all the retirement benefits) and commission based on fixed percentage of turnover achieved by the employee.

2.8.15 Exemption in Respect of amount received from various Provident Funds [Section 10(11)/ (12)] :

The tax treatment of various items in case of different provident funds is as follows :

1. Statutory Provident Fund: Employer's contribution to such fund is not treated as income of the employee. Interest credited to such fund is exempt in the hands of the employee. Amount received at the time of termination Lump sum amount received from such fund, at the time of termination of service is exempt in the hands of employees.
2. Recognized Provident Fund: Employer's contribution to such fund, up to 12% of salary is not treated as income of the Employee. Interest credited to such fund up to 9.5% per annum is exempt in the hands of the Employee, interest in excess of 9.5% is charged to tax in the hands of the employee. Amount received at the time of termination If certain conditions are satisfied, then lump sum amount received from such fund, at the time of termination of service, is exempt in the hands of employees.
3. Un-recognized Provident Fund: Employer's contribution to such fund is not treated as income of the employee. Interest credited to such fund is exempt in the hands of the employees. Amount received at the time of termination.
4. Public Provident Fund Employer's Contribution Employers do not contribute to such fund. Interest credited to such fund is exempt. Amount received at the time of termination Lump sum amount received from such fund at the time of termination of service is exempt from tax.

Notes:

- Salary for this purpose will include basic salary, dearness allowance, if the

terms of service so provide and commission based on fixed percentage of turnover achieved by the employee.

- Accumulated balance paid from a recognized provident fund will be exempt from tax in following cases:
- If the employee has rendered a continuous service of 5 years or more.
- If the service of employee is terminated before the period of 5 years, due to his ill health or discontinuation of business of the employer or other reason beyond his control.
- If on retirement, the employee takes employment with any other employer and the balance due and payable to him is transferred to his individual account in any recognized fund maintained by such other employer, then the amount so transferred will not be charged to tax. Except above situations, payment from a recognized provident fund will be charged to tax considering such fund as un-recognized from the beginning.

2.9 SUMMARY :

To determine taxable income, it is essential to find out residential status of the person and scope of total income. An individual or a HUF can be resident, not ordinarily resident or non -resident in India. All other assesses can be either resident or non-resident in India but cannot be not ordinarily resident in the matter of their residential status. Section 6 of the Income-tax Act prescribes the conditions to be fulfilled by various taxpayers to determine their residential status. The scope of total income and consequently the liability to income-tax depends upon

- Whether the income accrues or is received in India or outside
- The exact place and point of time at which the accrual or receipt of income takes place, and the residential status of the assessee.

Scope of Total income has been defined on the basis of Residential status Section 9 describes the various incomes which are deemed to accrue or arise in India. Exempted income means the income which is not at all charged to any taxes, while calculating the Gross Total Income. Whereas deduction means the amount which needs to be included in the income first then it is allowed for deduction in full or in part on fulfillment of certain conditions.

Exempted income means the income which is not at all charged to any taxes, while calculating the Gross Total Income. Deduction means the amount which needs to be included in the income first then it is allowed for deduction in full or in part on fulfillment of certain conditions.

2.10 KEY WORDS :

1. Resident :

An individual becomes a resident when he satisfies any one of the basic conditions. Other persons become resident on the basis of control and management.

2. Resident and ordinarily resident :

An individual or an HUF become ROR when the individual or the Karta of HUF satisfies both the additional conditions.

3. Resident but not ordinarily resident :

An individual or an HUF become RNOR when the individual or the Karta of HUF does not satisfy both the additional conditions.

4. Person of Indian origin :

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. It may be noted that grandparents include both maternal and paternal grandparents.

5. Income deemed to accrue or arise in India :

The incomes mentioned in section 9 of the Act, are deemed to accrue or arise in India.

2.11 SELF ASSESSMENT QUESTIONS :

1. How can you know whether a company is resident or non-resident?
2. How is resident/ non-resident status relevant for levy of income tax?
3. Under what circumstances an assessee will be considered "non-resident" for income-tax purposes and on what income he will be liable to be assessed?
4. In what way does the liability of tax of a "not ordinarily resident" person differ from that of a "resident" person under the Income-tax Act?
5. Give the exemptions under section 10.
6. What is tax incidence? How it can be determined?
7. How the tax Liability of different categories of assessee to be determined?
8. The dividend is declared and paid outside India. Discuss the tax liability on the transaction according to Indian income-tax on these dividends?

2.12 SUGGESTED READINGS :

1. R. K. Jain, Nikhil Gupta, Manoj Kumar Agrawal, Sanjeev S. Thakur, '*Practical Problems in Income Tax*', Scorer Guru Publications, Agra, 2023.

2. Dr. H. C. Mehrotra, Dr. S. P. Goyal, '*Problems and Solutions in Income Tax - Assessment Year 2022-23*', Sahitya Bhawan Publications, Agra, 2022.
3. Dr. H.C. Mehrotra, Dr. S.P. Goyal, '*Corporate Tax Planning & Management A.Y 2020-21 & 2021-22*', Sahitya Bhawan Publications, Agra, 2020.

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Lesson – 3

INCOME FROM SALARIES

Objectives :

After studying this unit, you should be able to

- To understand concept of salary and various important points regarding salaries;
- To know list of the items included under the head of salaries; and
- To learn the provisions of Income Tax Act, 1961 in relation to the Income from Salaries.

Structure of the lesson :

- 3.1 Introduction
- 3.2 History
- 3.3 Basis of Charge (Section 15)
- 3.4 Basic Elements of Salary
- 3.5 Definition of Salary [Sec. 17(1)]
- 3.6 Allowances
- 3.7 Perquisites [Section 17(2)]
- 3.8 Profits in Lieu of or in Addition to Salary (U/S 17(3))
- 3.9 Incomes Exempt from Tax and not includible In ‘Salary’
- 3.10 Deduction from Gross Salary [Sec. 16]
- 3.11 Computation of Salary, At a Glance
- 3.12 Summary
- 3.13 Keywords
- 3.14 Self-Assessment Question
- 3.15 Suggested Readings

3.1. INTRODUCTION :

Understanding the taxability of salary components and retirement benefits is crucial for both employees and employers in India. The Income Tax Act defines various elements of salary, allowances, and perquisites that are subject to taxation. Additionally, retirement benefits like gratuity, pension, and provident funds have specific tax implications.

A salary is a form of periodic payment from an employer to an employee, which may

be specified in an employment contract. It is contrasted with piece wages, where each job, hour or other unit is paid separately, rather than on a periodic basis. Salary can also be considered as the cost of hiring and keeping human resources for corporate operations, and is hence referred to as personnel expense or salary expense. In accounting, salaries are recorded in payroll accounts.

A salary is a fixed amount of money or compensation paid to an employee by an employer in return for work performed. Salary is commonly paid in fixed intervals, for example, monthly payments of one-twelfth of the annual salary.

Salaries are typically determined by comparing market pay-rates for people performing similar work in similar industries in the same region. Salary is also determined by leveling the pay rates and salary ranges established by an individual employer. Salary is also affected by the number of people available to perform the specific job in the employer's employment locale (supply and demand)

3.2 HISTORY :

While there is no first pay-stub for the first work-for-pay exchange, the first salaried work would have required a society advanced enough to have a barter system which allowed for the even exchange of goods or services between tradesmen. More significantly, it presupposes the existence of organized employers perhaps a government or a religious body that would facilitate work-for-hire exchanges on a regular enough basis to constitute salaried work. From this, most infer that the first salary would have been paid in a village or city during the Neolithic Revolution, sometime between 10,000 BCE and 6000 BCE.

Solariums :

Similarly, the Latin word *solariums* linked employment, salt, and soldiers, but the exact link is not very clear. More modern sources maintain instead that although Roman soldiers were typically paid in coin, the word *solariums* is derived from the word *sal* (salt) because at some point a soldier's salary may have been an allowance for the purchase of salt or the price of having soldiers conquer salt supplies and guard the Salt Roads (Via Salaria) that led to Rome. However, there is no ancient evidence for either of these hypotheses.

Some people even claim that the word soldier itself comes from the Latin *sal dare* (to give salt), but mainstream sources disagree, noting that the word soldier more likely derives from the gold solidus, with which soldiers were known to have been paid

Second Industrial Revolution :

From 1870 to 1930, the Second Industrial Revolution gave rise to the modern business corporation powered by railroads, electricity and the telegraph and telephone. This era saw the widespread emergence of a class of salaried executives and administrators who served the new, large-scale enterprises being created.

New managerial jobs lent themselves to salaried employment, in part because the effort and output of "office work" were hard to measure hourly or piecewise, and in part because they did not necessarily draw remuneration from share ownership.

As Japan rapidly industrialized in the 20th century, the idea of office work was novel enough that a new Japanese word (*salary man*) was coined to describe those who performed it, as well as referencing their remuneration

“Salary is the recompense or consideration given to a person for the pains he has bestowed upon another’s business” – Stroud’s Judicial Dictionary

3.3 BASIS OF CHARGE (SECTION 15) :

Section 15 deals with the basis of charge. Salary is chargeable to tax either on ‘due’ basis or on ‘receipt’ basis, whichever is earlier.

However, where any salary, paid in advance, is assessed in the year of payment, it cannot be subsequently brought to tax in the year in which it becomes due.

If the salary paid in arrears has already been assessed on due basis, the same cannot be taxed again when it is paid.

(1) Advance Salary : Advance salary is taxable when it is received by the employee irrespective of the fact whether it is due or not. It may so happen that when advance salary is included and charged in a particular previous year, the rate of tax at which the employee is assessed may be higher than the normal rate of tax to which he would have been assessed.

(2) Arrears of Salary : Normally speaking, salary arrears must be charged on due basis.

Points to consider :

- a) Salary income is chargeable to tax on “due basis” or “receipt basis” whichever is earlier.
- b) Existence of relationship of employer and employee is must between the payer and payee to tax the income under this head.
- c) Income from salary taxable during the year shall consist of following :
 - i. Salary due from employer (including former employer) to taxpayer during the previous year, whether paid or not;
 - ii. Salary paid by employer (including former employer) to taxpayer during the previous year before it became due;
 - iii. Arrear of salary paid by the employer (including former employer) to taxpayer during the previous year, if not charged to tax in any earlier year;

Exceptions - Remuneration, bonus or commission received by salary to partners from the firm is not taxable under the head Salaries rather it would be taxable under the head business or profession.

Provision illustrated :

Mr. X joined A Ltd. for a salary of Rs.5,000 p.m. on 1/4/2020. In the year 2021-22, his increment decision was pending. On 1/4/2020, his increment was finalized as for 2019-20: 1,000 p.m. and for 2022-23 Rs.1,500 p.m. Such arrear salary received on 5/4/2023. Find Gross taxable salary. Further, salary of April 2023 has also been received in advance on 15/03/2021.

Solution :**Calculation of Gross taxable salary for the Assessment Year 2023-24**

Particulars	Workings	Amount (Rs.)
Salary for 2022-23	$(5,000 + 1,000 + 1,500) * 12$	90,000
Arrear salary for 2021-22	$(1,000) * 12$	12,000
Advance salary for April 2023		7,500
Gross total salary		1,09,500

Salary due Vs. Salary accrued :

Salary due is different from salary accrued.

Example: Mr. X joined an organisation for Rs.10,000 p.m. on 1st Dec. 2020, in which salary falls due on 1st day of every next month. In such case taxable salary for the Assessment Year 2023-24 shall be Rs.30,000 calculated as under :

Month	Amount of Salary (Rs.)	Due date of salary	Taxable in the P.Y.
Dec 2022	10,000	1/1/2022	2021-22
Jan 2023	10000	1/2/2022	2021-22
Feb 2023	10000	1/3/2022	2021-22
Mar 2023	10000	1/4/2022	2022-23

Advance salary Vs. Advance against salary :

‘Advance salary’ is taxable U/s17 (1)(e) whereas ‘Advance against salary’ is treated also as hence, not taxable under the head “Salaries”.

Place of accrual of salary :

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

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

Exceptions :

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

Tax point : Salary is earned at the place where service is rendered.

Employee	Employer	Place of service	Salary received	Taxable
Any	Any	India	Any where	Yes
Any	Any	Any where	India	Yes
Ordinarily resident	Any	Any where	Any where	Yes
Indian citizen	Government	Outside India	Any where	Yes
Not ordinarily resident/Non resident	Any	Outside India	Outside India	No

3.4 BASIC ELEMENTS OF SALARY :

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

Employer-employee relationship :

A payment can be construed as salary only if the payer is the employer and payee is the employee of the payer.

- **Criteria for employer-employee relationship:** The key criteria to hold this relationship is that, employee are always bound to work as per direction and supervision of the employer.
- **Payment in employer's capacity:** To treat any payment as salary it is necessary that payer, being the employer, must have made the payment in such (employer's) capacity.
- **Contract of service vs. contract for service:** In "contract of service", the employer can direct and control the duties and the manner of performance of employee hence employer-employee relationship exists in such contract. However, in case of "contract for service" the contract can simply decide and quote the objector target to be achieved but cannot decide or direct the manner of performance.
- **Agent and Principal:** If a person is acting as an agent for his principal, any

commission or remuneration earned by the agent is not taxable under the head “Salaries”. This is because; an agent is not the employee of his principal.

- Salary received by a partner from its firm shall not be taxable as salary, because there is no employer-employee relationship between the firm and the partner. Such salary shall be taxable under the head “Profits & gains of business or profession”.
- Salary received by proprietor from his proprietorship firm is not an income. As proprietor and proprietorship firm are the same person and no one can earn from himself.
- Remuneration to director from his company can be treated as salary only if the director is employee of the company, otherwise the same shall be taxable under the head “Income from other sources”.

Note : Directors’ sitting fee is taxable under the head “Income from other sources”.

- Pension received by the widow or legal heir of deceased employee is not taxable as salary as no employer employee relationship exists between the payer and the payee. However such amount shall be taxable under the head “Income from other sources”.
- Remuneration received by Judges is taxable under the head “Salaries” even though they are not having any employer.

Concluding the above discussions, a payment received for services rendered, from a person other than employer, is not taxable under the head “Salaries” but may be taxed under the head “Profits & gains of business or profession” or “Income from other sources”.

Sections	Topics covered under these sections
Section 15	Basis of Charge
Section 16	Deductions from Salary
Sec.17 of Income Tax Act, 1956 deals with the Income from Salaries	Income from Salaries
Sec.17(1)	Definition of Salary Income
Sec.17(2)	Perquisites
Sec.17(3)	Profits in lieu of Salary

3.5 DEFINITION OF SALARY [SEC. 17(1)] :

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

- a) Wages;
- b) Any annuity or pension;
- c) Any gratuity;

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

3.6 ALLOWANCES :

All monetary payments made by an employer to his employees, other than salary, are termed as allowance. It is fixed, predetermined, and given regularly in addition to salary in connection with the services rendered by the employee. It may be given in form of reimbursement of some expenditure incurred by the employee or may be given irrespective of actual expenditure. From the income tax view point, all the allowances may be classified in three parts, i.e. Fully taxable, partially exempted and fully exempted.

ALLOWANCES

Fully taxable	Partially exempted	Fully exempted
1) Dearness Allowance or Dearness Pay	1) House Rent Allowance	1) Conveyance Allowance
2) Medical Allowance	2) Entertainment Allowance	2) Foreign Allowance
3) Tiffin Allowance	3) Travel Allowance	3) Allowances to High Court Judges
4) Servant Allowance	4) Special Allowance exempt	4) Allowance from UNO
5) Non-Practicing Allowance	u/s 10(14)(ii):	5) Special Allowance notified
6) Warden Allowance	a) Children Education Allowance	U/S 10(14)(i):
7) Deputation Allowance	b) Hostel Allowance	a) Tour allowance
8) Overtime Allowance	c) Composite hill Allowance	b) Daily Allowance
9) City Compensatory Allowance	d) Tribal Area Allowance	c) Conveyance Allowance for performance of official duty
10) Other Allowances:	e) Allowance for meeting personal expenditure to an employee of transport	d) Helper allowance
i) Shift allowance		e) Academic allowance
ii) Marriage allowance		f) Uniform allowance
iii) Project allowance		

	<p>organization while on duty during the running of such transport</p> <p>f) Border Area Remote Area, Difficult Area, or Disturbed Area Allowance</p>	
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Fully Taxable Allowances :

Fully taxable allowances which are shown in the table received by an employee from his employer are included fully in his salary income to ascertain his tax liability.

Partially Exempted Allowances :

The allowances which are partially exempted, and remaining part is taxable treated under this category. The taxable portion is ascertained as below :

(A) House Rent Allowance [Sec 10 (13A)] :

Generally, employees receive house rent allowance from their employers to meet the expenditure incurred by them towards house rent. It is exempt from tax subject to the following limits: Least of the following is exempt from tax:

- (i) Actual House Rent Allowance received by the employee in respect of the relevant period; or
- (ii) Rent paid by the employee in excess of 10% of salary due to him in respect of the relevant period; or
- (iii) 50% of salary due to him in respect of the relevant period if the accommodation is situated at Mumbai, Kolkata, Delhi, or Chennai; or
- (iv) An amount equal to 40% of the salary due to him in respect of the relevant period if the accommodation is situated at any other place.

The least amount is exempt from tax and the remaining amount shall be taxable and is included in the gross salary.

Quantum of exemption: Minimum of following three limits :

Mumbai/Kolkata/Delhi/Chennai	Other cities
1. Allowance actually received	Allowance actually received
2. Rent paid in excess of 10% of salary	Rent paid in excess of 10% of salary
3. 50% of salary	40% of salary

Note : i) Meaning of salary = Basic salary + Dearness allowance (if it is under the terms of employment) + commission at fixed rate on sale.

(B) Entertainment Allowance :

It is paid by an employer to his employee to compensate for entertainment expenses. The total amount is firstly included in his salary income and at last if employee fulfils certain conditions, it is allowed as deduction.

(C) Transport Allowance :

Transport allowance is taxable for normal person from A.Y. 2019-20 but for blind or deaf or dumb or orthopedically handicapped with disability of lower extremities, it will be exempt up to Rs. 3,200 p.m.

(D) Special Allowances :

Specifically exempted u/s 10 (14) (ii) notification No. SO 259(5) dated 27-3-1990 have notified the following allowances :

- i) Special Compensatory Hilly area allowance or High-Altitude allowance or uncongential climate allowance or snow bound area allowance or Avalanche allowance** is exempt from tax up to maximum of Rs. 300 p.m., if employee is working at height 1,000 meter or above the sea-level.

The prescribed limit depends upon the height of the regions, Rs. 7,000 for Siachen area of Jammu & Kashmir or Rs. 800 p.m. for other hill areas (located at height of more than 9,000 feet).

- ii) Border area allowance or remote area allowance or difficult area allowance or disturbed area allowance** is exempt at the following rates:

- a. Andaman, Nicobar and Narcondum islands some specified places of north, some specified places of Himachal Pradesh, and areas beyond 25 km from Lungali district of Mizoram - Rs. 1,300 p.m.
- b. Continental shelf of India and exclusive economic zone of India- Rs. 1,100 p.m.
- c. Arunchal Pradesh, Jammu and Kashmir, district Lungali of Mizoram, Nagaland, Tripura, South Andaman, some areas of Himachal PradeshRs. 1,050 p.m.
- d. Uttar Pradesh, Haryana, Rajasthan, Punjab, Aizawal district of Mizoram, some areas of Jammu and Kashmir, Tripura, Manipur, Himachal Pradesh- Rs. 750 p.m.
- e. Jog falls in district Shimoga of Karnataka - Rs. 300 p.m.
- f. Some areas of Himachal Pradesh, throughout Assam and MeghalayaRs. 200 p.m.

- iii) Tribal allowance :**

This exemption is available @ Rs. 200 per month in nine States (i) Madhya Pradesh

(ii) Tamil Nadu (iii) Uttar Pradesh (iv) Karnataka (v) Tripura (vi) Assam (vii) West Bengal (viii) Bihar and (ix) Orissa.

- iv) Any allowance granted to an employee working in any transport system** to meet his personal expenditure during his duty performed while running of such transport from one place to another place in India, is exempt up to a specified limit. The specified limit is 70% of such allowance or Rs. 10,000 p.m. (whichever is less)
- v) Children educational allowance:** It is exempt @Rs. 100 per month per child up to a maximum of two children.
- vi) Hostel expenditure allowance:** Any allowance granted to an employee to meet the hostel expenditure on his child @ Rs. 300 p.m. per child up to a maximum of two children.
- vii) Compensatory field area allowance:** Exempt to the extent of Rs. 2,600 per month (Specified areas of Jammu and Kashmir, Uttar Pradesh, Himachal Pradesh, Manipur, Nagaland, specified areas of Arunachal Pradesh).
- viii) Counter insurgency allowance:** Exempt to the extent of Rs. 3,900 per month. This allowance is granted to members of armed forces operating in areas away from their permanent location for a period of more than 30 days.
- ix) Underground allowance:** Such allowance is granted to an employee who is working in uncongenial climate in underground coal mines and shall be exempt to the extent of Rs. 800 per month.
- x) High altitude allowance:** Given to the members of armed forces for altitude of 9000 feet to 15000 feet, is exempt upto Rs. 1,060 per month and for altitude above 15000 feet, Rs. 1,600 per month.
- xi) Special compensatory highly active field area allowance:** Such allowance is given to the members of armed forces and is exempt upto the extent of Rs. 4,200 per month.
- xii) Island (duty) allowance:** Given to the member of the armed forces in Andaman & Nicobar and Lakshadweep Group of Islands and is exempt upto the extent Rs. 3,250 per month.
- xiii) Compensatory modified field area allowance:** Exempt upto the extent of Rs. 1,000 per month (Specified area of Punjab, Rajasthan, Haryana, Himachal Pradesh, Arunachal Pradesh, Assam, Mizoram, Tripura, Sikkim, West Bengal Uttar Pradesh, Specified Areas of Jammu and Kashmir)

3.7 PERQUISITES [SECTION 17(2)] :

The term “perquisites” includes all benefits and amenities provided by the employer to the employee in addition to salary and wage either in cash or in kind which are convertible

into money. These benefits or amenities may be provided either voluntarily or under service contract.

The term “Perquisite” is defined by section 17(2) as follows :

- (i) The value of rent-free accommodation provided to the assessee by his employer;
- (ii) The value of any concession in the matter of rent respecting any accommodation provided to the assessee by his employer;

For income-tax purposes, the perquisites are of three types:

- (A) Tax-free perquisites
- (B) Taxable perquisites
- (C) Perquisites taxable under specified cases.

(A) Tax-free perquisites (in all cases) :

The value of the following perquisites is not to be included in the salary income of an employee :

i. Medical Facilities :

- The value of any Medical facility provided to an employee or his family member in any hospitals, clinics, etc. maintained by the employer.
- Reimbursement of expenditure actually incurred by the employee on medical treatment for self or for his family members in any hospitals, dispensaries etc. maintained by the Government or local authority or in a hospital approved under the Central Health Scheme or any similar scheme of the state Government or in a hospital, approved by the chief commissioner having regard to the prescribed guidelines for the purposes of medical treatment of the prescribed diseases or ailments.
- Group medical insurance obtained by the employer for his employees (including family members of the employees) or all medical insurance payments made directly or reimbursement of insurance premium to such employees who take such insurance.
- Reimbursement of medical expenses actually incurred by the employee upto a maximum of ` 15,000 in the aggregate in a year, in a private hospital for his and his family.
- Any expenditure incurred or paid by the employer on the medical treatment of the employee or any family member of the employee outside India, the travel and stay abroad of such employee or any family member of such employee or any travel or stay abroad of one attendant who accompanies the patient in connection with such treatment will not be included in perquisites of the employee. However, the travel expenditure shall be excluded from the perquisites only when the employee’s gross total income as computed before

including the said expenditure does not exceed two lakh rupees and further to such conditions and limits as the Board may prescribe having regard to guidelines, if any, issued by the Reserve Bank of India.

ii. Refreshment :

The value of refreshment provided by the employer during office hours and in office premises is fully exempt. Free Meals provided by the employer during working or business hours or through paid nontransferable (usable only at eating joints) voucher if its value thereof in either case does not exceed `50 will not be treated as income of the employee. However, free meals provided by the employer during working hours in a remote area or an offshore installation shall be fully exempt.

iii. Subsidized lunch or dinner provided by employer :

Expenditure incurred by employer on provision of food or beverages to employees either inside or outside the place of work during working hours upto 35 per day per employee will not be treated as income of the employee provided the amount is paid by the employer directly to the caterer, restaurant, eating place, canteen, etc.

iv. Recreational facilities:

The value of recreational facilities provided is exempt.

v. Telephone facility provided at the residence of the employee is exempt to the extent of the amount of telephone bills paid by the employer when it is used for official and personal purposes of the employee.

vi. The value of transport provided by the employer to the employees as a group (and not to any individual or a few employees alone) from their place of residence to the place of work and back in the case of an employer engaged in the business of carriage of goods or passengers, to his employees either free of charge or at a concessional rate. Conveyance facility provided for the journey between office and residence and back at free of charge or at concessional rate.

vii. Personal accident insurance: Payment of annual premium by employer on personal accident policy affected by him to his employee.

viii. Fresher Course: Where the employee attends any refresher course in management and the fees are paid by the employer, the amount spent by employer for the purpose.

ix. Free rations: The value of free rations given to the armed forces personnel.

x. Family planning: The amount spent by an employer on the promotion of family planning amongst its employees.

xi. Sale of an asset(being a movable asset but other than car, electronic items) or gift of such asset to an employee after using the same by the employer for 10 years or more is a perquisite in the hands of employee.

- xii. Perquisites to Government employees being citizens of India, posted abroad.
- xiii. Rent-free house to High Court Judges
- xiv. Rent-free house to Supreme Court Judges
- xv. Conveyance facility to High Court and Supreme Court judges.
- xvi. Privilege passes and privilege ticket orders granted by Railways to its employees.
- xvii. Sum payable by an employer through a recognized Provident Fund or an Approved Superannuation Fund or Deposit-linked Insurance Fund established under the Coal Mines Provident Fund or the Employees' Provident Fund.
- xviii. Sum payable by an employer to pension or deferred annuity scheme.
- xix. Employer's contribution to staff group insurance scheme.
- xx. Actual travelling expenses paid/reimbursed by the employer for journeys undertaken by employees for business purposes.
- xxi. Leave travel concession exempt as per provision of Section 10.
- xxii. Free holiday trips to non-specified employees.
- xxiii. Rent-free furnished residence (including maintenance thereof) provided to an Officer of Parliament, a Union Ministry and a leader of opposition in Parliament.
- xxiv. Goods sold to employees, by their employer, at concessional rates.
- xxv. The value of any benefit provided by a company free of cost or at a concessional rate to its employees by way of allotment of shares, debentures or warrants directly or indirectly under the Employees' Stock Option Plan or Scheme of the said company.
- xxvi. Free educational facility to the children of the employee in an educational institute owned/maintained by the employer if cost of such education or value of such benefit does not exceed ` 1,000/- per month per child.
- xxvii. Interest free loan to an employee if the amount of loan does not exceed `20,000/- or if loan is provided for specified diseases.
- xxviii. Computer/laptops (provided only for use, ownership is retained by the employer).

(B) Taxable perquisites (in all cases) :

The value of the following perquisites is added to the salary income of the employee:

- i. Value of rent-free residential accommodation provided to the assessee (except to the Judge of a High Court or Supreme Court; an Officer of Parliament, a Union Minister and a leader of opposition in Parliament).
- ii. Value of any concession in the matter of rent in respect of residential accommodation provided to the assessee.

- iii. Sum paid by the employer (directly or indirectly) for effecting an assurance on the life of the employee or for providing an annuity. If the amount is paid to a recognized provident fund or an approved superannuation fund, or to a deposit linked insurance fund established under the Coal Mines Provident Fund Act or Employees' Provident Fund Act, the sum so paid is not to be included in the salary income.
- iv. Sum paid by the employer in respect of any obligation of the assessee, which would otherwise have been payable by the assessee. Some of the examples of such expenses are as follows:
 - v. Income-tax paid by the employer due from the employee.
 - vi. Payment of club bills, club subscription or hotel bills of the employee.
 - vii. Fees paid by the employer directly to the school or reimbursement of tuition fees of the children of the employee.
 - viii. Payment of any loan due to the employee.
 - ix. 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.
 - x. The amount of any contribution to an approved superannuation fund by the employer in respect of the assessee, to the extent it exceeds one lakh rupees;
 - xi. The value of any other fringe benefit or amenity as may be prescribed.

(C) Perquisites taxable only in the cases of Specified Employees :

The value of certain benefit or amenity granted or provided free of cost or at a concessional rate in any of the following cases only shall be included in the salary income:

- i. By a company to an employee who is director thereof [It is immaterial whether the director is full time or part time director];
- ii. By a company concern to an employee, being a person who has a substantial interest in the company concern, i.e., employee is the beneficial owner of at least 20 per cent of the equity shares of that company or is entitled to at least 20 per cent share in profit of the concern;
- iii. An employee whose income chargeable under head salaries (exclusive of the value of all benefits or amenities not provided by way of monetary payments) exceeds ` 50,000, is a specified employee.
- iv. Some of the examples of such perquisite which are included in the salary income of a specified employee as defined above are:
 - v. Free boarding facility provided by employer.
 - vi. Free conveyance for private use.

- vii. Free education facility to the family members of employee.
- viii. Holiday trips at employer are cost.
- ix. Gas, electricity or water supplied free for household consumption.
- x. Wages of domestic servants paid by employer.
- xi. Free lunches or dinners

3.8 PROFITS IN LIEU OF OR IN ADDITION TO SALARY (U/s 17(3)) :

Under this the following items are included :

- The amount of any compensation due to or received by an assessee from the employer or former employer at or in connection with the termination of his employment. The 'termination of employment' means retirement, premature termination of employment, termination by death or voluntary resignation
- The amount of any compensation due to or received by any assessee from his employer in connection with the modification of the terms and conditions relating to employment. For example, where an employer
 - wants to cut down the salary payable to the employee, the lump sum paid to compensate the employee shall be treated as profits in lieu of salary
- 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;
 - (B) Or (B) after cessation of his employment with that person.
- Any payment other than the following payment due to or received by assessee from an employer or a former employer or from a provident or other fund, to the extent to which it does not consist of contribution by the assessee or interest on such contributions by the assessee or interest on such contributions or any sum under key man Insurance Policy.

3.9 INCOMES EXEMPT FROM TAX AND NOT INCLUDIBLE IN 'SALARY' :

The following items relevant to salaries have been discussed under Incomes which do not form part of total income and are exempt from tax, subject to the limits applicable for each :

1. Leave Travel Allowance [Section 10(5)];
2. Remuneration of a person who is not a citizen of India [Section 10(6)].
3. Allowances payable outside India [Section 10(7)];
4. Remuneration of an employee working under the Co-operative Technical Assistance Programme [Section 10(8)];

5. Death-cum-retirement gratuity [Section 10(10)];
6. Amount received in commutation of Pension [Section 10(10A)];
7. Encashment of earned leave [Section 10(10AA)];
8. Retrenchment compensation [Section 10(10B)];
9. Payment received from Statutory Provident Fund [Section 10(11)];
10. Payment received from a recognized Provident Fund [Section 10(12)];
11. Payment received out of an approved Superannuation Fund [Section 10(13)];
12. House rent allowance [Section 10(13A)];
13. Special allowances to meet the expenses of the duties [Section 10(14)];
14. Salary income of a member of Scheduled Tribe [Section 10(26)];
15. Salary income of a resident of Ladakh [Section 10(26A)];

3.10 DEDUCTION FROM GROSS SALARY [SEC. 16] :

3.10.1 Standard Deduction [SEC. 16(IA)] :

Standard Deduction [Sec. 16(ia)]

Lower of the following shall be allowed as standard deduction to all employees :

- a. Rs. 50,000
- b. Amount of gross salary

3.10.2 Entertainment Allowance [SEC. 16(ii)] :

Entertainment allowance is initially included in taxable allowances as fully taxable. Thereafter, a deduction is allowed under this section from gross taxable salary. However, deduction u/s 16(ii) shall be available to the Government employee only. Deduction for Entertainment allowance being minimum of the following:

- A. Actual Entertainment Allowance
- B. Rs. 5,000/-
- C. 20% of Basic Salary.

Tax point :

- Deduction allowed shall be irrespective of actual expenditure incurred, whether for office or personal purpose.
- No deduction is available under this section to a Non-government employee.

Illustration :

Compute taxable Entertainment allowance & net salary of Sri Hanuman Prasad from the following data :

Income Tax	3.17	Income From Salaries
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Basic salary Rs.8,000 p.m.

D.A. Rs.2,000 p.m.

Taxable perquisite Rs.35,000,

Entertainment Allowance Rs. 4,000 p.m.

Out of such allowance Rs.20,000 is expended and balance amount is saved.

Assuming he is: a. Government employee b. Non-Government employee.

Particulars	Government Employee		Private Employee	
	Details	Amount (Rs.)	Details	Amount
Basic Salary		96,000		96,000
Dearness Allowance		24,000		24,000
Entertainment Allowance		48,000		48,000
Taxable perquisite		35,000		35,000
Gross Taxable Salary		2,03,000		2,03,000
Less: Deduction u/s				
16(ia) Standard Deduction	50,000		50,000	
16(ii) Entertainment allowance#	5,000	55,000	Nil	50,000
Net Taxable Salary		1,48,000		1,53,000

Working Notes

* Entertainment Allowance is exempted to the extent of minimum of the following:

- Actual Entertainment Allowance Rs.48,000.
- 20% of Basic Salary Rs.19,200.
- Statutory amount Rs.5,000.

3.10.3 Tax on Employment or Professional Tax [SEC. 16(iii)] :

Tax on employment, profession, trade, etc. levied by a State under Article 276 of the Constitution will be allowed as deduction on cash basis, whether paid by employee or by employer (on behalf of employee) from gross taxable salary.

Note :

If employer (on behalf of employee) pays Professional tax then :

- Firstly, it is to be included as taxable perquisite; and
- Further, it is allowed as deduction u/s 16(iii).

Illustration :

Mr. Rohit a non-Government employee has the following salary details :

- a. Basic Salary Rs.5,000 p.m.
- b. D.A. Rs.2,000 p.m.
- c. Entertainment Allowance Rs.300 p.m.
- d. Professional tax paid by employee Rs.600
- e. LIC Premium paid by employer Rs.3,600
- f. Income tax paid by employee Rs.2,000
- g. Professional tax paid by employer on behalf of employee Rs.1,600

Find his taxable salary.

Solution :

Computation of taxable salary Mr. Rohit for the A.Y.2021-22

Particulars	Details	Amount (Rs.)
Basic Salary		60,000
Allowances		
Dearness Allowance	24,000	
Entertainment Allowance	3,600	27,600
Taxable perquisite		
Professional tax paid by employer	1,600	
LIC Premium paid by employer	3,600	5,200
Gross Taxable Salary		92,800
Less: Deduction u/s		
16(ia) Standard Deduction	50,000	
16(ii) Entertainment allowance (Assessee is a Non-government employee)	Nil	
16(iii) Professional Tax (` 1,600 + ` 600)	2,200	52,200
Taxable Salary		40,600

B. Meaning of Salary for different purposes :

For Retirement benefit	
Gratuity (covered by the Payment of Gratuity Act)	(Basic + DA) last drawn
Gratuity (not covered by the Payment of Gratuity Act)	(Basic + DA ¹ + Commission ²) being average of last 10 months preceding the month of retirement

Leave encashment	(Basic +DA ¹ + Commission ²) being average of last 10months immediately from the retirement.
Voluntarily retirement	(Basic +DA ¹ + Commission ²) last drawn
For regular benefit	
Rent Free Accommodation	(Basic + DA ¹ + Commission ² + Bonus + Fees + Any other taxable allowance + Any other monetary benefits excluding perquisite)
Specified employee	(Basic + DA + Commission ² + Bonus + Fees + Any other taxable allowance + Any other monetary benefits –Deduction u/s 16)
Entertainment Allowance	Basic only
Any other case	(Basic +DA ¹ + Commission ²)

1. DA only if it forms a part of retirement benefit.
2. Commission as a fixed percentage on turnover.

3.11 COMPUTATION OF SALARY, AT A GLANCE :

Computation of income under the head “Salaries” of for the A.Y.

Particulars	Details	Amount
Basic Salary		*****
Fees		*****
Commission		*****
Bonus		*****
Gratuity		*****
Leave Encashment		*****
Pension		*****
Retrenchment Compensation		*****
Compensation received under Voluntary Retirement Scheme		*****
Allowances:		
Dearness Allowance (DA) /Dearness Pay (DP)	*****	
House Rent Allowance	*****	
Children Education Allowance	*****	
Children Hostel Allowance	*****	
Entertainment Allowance	*****	
Medical Allowance	*****	
Conveyance Allowance	*****	

Conveyance Allowance	*****	
City Compensatory Allowance	*****	
Uniform Allowance	*****	
Professional Development Allowance	*****	
Transport Allowance	*****	
Other Allowances	*****	*****
Perquisites u/s 17(2)		
Any Obligation of Employee paid by Employer	*****	
Accommodation	*****	
Shares and securities issued under ESOP	*****	
Employer's Contribution to Superannuation Fund	*****	
Gas, Electricity & Water	*****	
Medical Facility	*****	
Other fringe benefits	*****	*****
Leave Travel Concession		*****
Contribution of Employer to Provident Fund		*****
Interest on Recognised Provident Fund		*****
Any other item		*****
Gross Salary		
Less: Deduction u/s 16		
(ia) Standard Deduction	*****	
(ii) Entertainment Allowance	*****	
(iii) Tax on employment/Professional tax	*****	*****
Taxable Salary		*****

3.12 SUMMARY :

Income from salary is one of the main heads of income. Salary means any remuneration paid by the employer to the employee for service rendered. The meaning of salary for tax purpose is very wide. It not only includes the cash received but also the monetary value of facilities and benefits attached with the office of employment. It includes salary or wages, bonus, pension, annuity, gratuity, leave encashment, advance, fees or commission, contribution to provident fund, profit in lieu of salary.

In order to calculate the taxable salary of an individual, the taxable amount of all the above items is to be calculated and added together. The term salary is not only wide but has many meaning. 'Salary' includes different items for different purpose, for example, while calculating the encashment of earned leave 'salary' means basic salary, dearness allowance if terms of employment so provide and commission, if based on fixed percentage of turnover. For calculating gratuity and HRA, 'salary' includes basic salary, DA, if terms of employment so provide, dearness pay and commission, if based on fixed percentage of turnover.

3.13 KEYWORDS :

1. Advance Salary :

This is salary received for services yet to be rendered, and is taxable on receipt basis.

2. Allowance :

Monetary benefits attached to an office or employment like conveyance allowance, HRA, etc for meeting particular requirements connected with the services rendered by the employee or compensation for unusual conditions of service.

3. Commutation of Pension :

A retired employee who is in receipt of pension can choose to forego a part of his pension in future, in lieu of which, he can get a lump sum. This is known as commutation. Exemption is available in respect of such commutation subject to limits.

4. Encashment of Earned Leave :

Usually, employees get 30 days of earned leave in a year which can be accumulated. Generally, all organization allows their employees to encash their earned leave, if the accumulation exceeds a prescribed limit. Leave encashed during service period is taxable while leave encashed on retirement is exempt subject to certain limits.

5. Gratuity :

This is a lump sum payment paid to an employee, usually at the time of retirement in recognition of long and meritorious service. Exemption is available subject to certain limits.

6. Pension :

This is a monthly payment received by a retired employee from his former employer. This is taxable as salary income.

7. Profits in Lieu of Salary :

The Income Tax Act treats certain items like compensation received by an employee on termination of his employment, certain payment from unrecognized provident fund and all other payment made by an employer or former employer as profits in lieu of salary. These are taxable as salary income.

3.14 SELF ASSESSMENT QUESTIONS :

1. What are the provisions of Income Tax Act regarding commutation of pension?
2. Discuss about various allowances allowed to employees.
3. What are the provisions for calculating House rent allowance?
4. What do you mean by profit in lieu of salary?

3.15 SUGGESTED READINGS :

1. R. K. Jain, Nikhil Gupta, Manoj Kumar Agrawal, Sanjeev S. Thakur, '*Practical Problems in Income Tax*', Scorer Guru Publications, Agra, 2023.
2. Dr. H. C. Mehrotra, Dr. S. P. Goyal, '*Problems and Solutions in Income Tax - Assessment Year 2022-23*', Sahitya Bhawan Publications, Agra, 2022.
3. Dr. H.C. Mehrotra, Dr. S.P. Goyal, '*Corporate Tax Planning & Management A.Y 2020-21 & 2021-22*', Sahitya Bhawan Publications, Agra, 2020.
4. J.C. Varshney & Nikhil Gupta, "Corporate Tax Planning", SBPD Publication, Agra, 2022.

G. David Raju

Lesson – 4
COMPUTATION OF INCOME FROM SALARIES
(Problems)

Objectives :

The objectives of the lesson are to acquire knowledge about Computation of Income from Salaries and allowable deductions.

Structure of the lesson :

- 4.1 Solved Illustrations on Computation of Income from Salaries
- 4.2 Summary
- 4.3 Keywords
- 4.4 Self Assessment Illustrations
- 4.5 Suggested Readings

4.1 SOLVED ILLUSTRATIONS ON COMPUTATION OF INCOME FROM SALARIES :

Illustration – 1 :

If Mr. Dinesh Varma(Non-Government employee) has a salary of Rs. 30,000 per month with DA of Rs. 4500 per month, entertainment allowance of Rs. 2250 per month and pays Rs.3500 towards professional tax, then his taxable income would be calculated as follows :

Particulars		Amount
Basic Salary	30000x12	3,60,0000
DA	4500x12	54,000
Entertainment Allowances	2250x12	27,000
Gross Salary		4,41,000
Standard Deductions u/s 80	50,000	
Professional Tax	3,500	53,500
Net Salary		3,87,500
Tax Slab 2,50,001 – 5,00,000 - 5% above 250,0000 387,500-250,000=187,500x5% = 6875		6,875
Rebate u/s 87A: Resident Individual whose Total Income is not more than Rs.5,00,000 is also eligible for a Rebate of up to 100% of income tax or Rs.12,500, whichever is less. This Rebate is available in both tax regimes.		

*Entertainment allowance exemption not available in case of non- government employee.

As his taxable income is Rs. 3,87,500 he falls in the slab of 2.5 lakhs – 5 lakhs of income tax as per the old tax regime. Thus he has to pay 5% of his net income as income tax + 4% cess. Income tax on the above net income = 6875/- but rebate u/s 87A is allowed up to Rs 12,500/- for income less than Rs 5 lakhs therefore no tax on income of Rs 3,87,500/-

Tax Planning for a salaried individual :

Tax Planning is a tax saving by using the exemptions given by the Income Tax Act. Through the given exemptions, an assessee can avoid the tax. Hence the tax avoidance is nothing but tax planning.

To reduce taxes, it is highly important to understand the salary structure :

Taxable Salary Income = Salary – Exemptions (Exempt allowances + Standard deduction + Professional Tax)

Net taxable income = Taxable Salary Income – Deductions

Every citizen wants to increase the income and at the same time pay lesser tax. There are some ways to do this. These tax savings methods save money for your future and also saves a significant amount on the income tax. Some of the most popular tax savings instruments are :

ELSS :

Equity Linked Savings Schemes are equity mutual funds with distinctive features. ELSS qualify below section 80C and are exempted up to 1.5 lakhs. They have a 3-year lock-in period and are offered by almost every mutual fund company. The returns are based upon the market changes and that is why there is no fixed return rate on ELSS. But these returns from ELSS are completely tax-free which, is the major driving force for people to choose investment in ELSS.

PPF :

Public Provident Fund (PPF) is also a very popular method of investment. Since its launch, PPF has been the preferred method of investment and tax savings for millions of salaried individuals. Being a government scheme, it enjoys a lot of trust from people. PPF gives interest at a fixed rate, which currently is 7.1%. The maximum limit for investing in PPF is 1.5 lakhs, while the minimum limit is INR 500 annually. PPF has a lock-in period of 15 years, which can be extended in the block of 5 years. PPF is the best option for people who do not like volatility in their investments and want to invest in safe options.

ULIP :

ULIP or Unit Linked Insurance Plan is a hybrid of insurance plans and market-linked investments. With a lock-in period of 5 years, it offers both protection and savings. The lock-in period can be extended up to 15 and even 20 years. There are 9 fund options in ULIP between which an investor can switch at any time, and the returns on them are completely tax-free.

Deductions under section 80 :

Under section 80 of the Income Tax Act, 1961, many deductions are available, which bring down the taxable income for an individual and thus reduce the tax payable.

These deductions are :

Section	Maximum Limit	Deductions
Section: 80C	1,50,000	ULIP, ELSS, NSC(National Saving Certificate), the Employee share of PF, LIC Premium, Children's tuition fees, Home loan principal repayment, 5-year tax saving FD , purchasing of a deferred annuity, Senior citizen's saving scheme (SCSS), Sukanya Samriddhi Yojana (SSY), Pension fund set up by UTI or mutual fund, annuity plan of LIC, Subscription to Home Loan Account
Section: 80CCC	NA	
Section: 80CCC	NA	On the amount deposited in the annuity plan of LIC or any other insurance plan for a pension fund.
Section: 80CCD(1)	- 1,50,000 -10% of salary (in case taxpayer is employee) -20% of gross total income (in case of self-employed) Least of the above	Employee's contribution to NPS account
80CCD(2)	10% salary	Employer's contribution to NPS
Section: 80CCD(1b)	50,000	Any other contribution to NPS by employee
80TTA(1)	10,000	Income from interest earned on savings account
80TTB	50,000	Interest received from banks, post office, etc. but

		applicable only to senior citizens
Section: 80GG	5000 per month / 25% of adjusted total income rent paid – 10% of adjusted total income (W.E.L.)	For rent paid when HRA is not received from an employer
Section: 80E	Amount equal to the interest paid every year (for maximum 8 years)	Interest paid on education loan
Section: 80EE	50,000	Interest paid on home loans by the first time homeowners subject to specified conditions
Section: 80D	25,000	Medical insurance of self, spouse and children
Section: 80D	50,000	Medical insurance of parents over 60 years or uninsured parents over 80 years of age.
80DD	75,000	Medical treatment of handicapped dependent
Section: 80DD	75,000 (40%-80% disability), ` 1,25,000 (more than 80%)	Payment made to specific scheme taken for the maintenance of handicapped dependent
Section: 80DDB	40,000 or the amount paid (w.e.l.)	Medical expense on self or dependent less than 60 years old
Section: 80DDB	1,00,000 or the amount paid (w.e.l.)	Medical expense on self or dependent more than 60 years old
Section: 80U	1,25,000 (severe disability), ` 75,000 (less severe disability)	Self-suffering from physical disability including blindness and mental instability
Section 80 G	NA	various donations specified in u/s 80G are eligible for deduction up to either 100% or 50% with or without restriction

Section: 80GGB	Contributed amount (Not in cash)	Contribution made to political parties by companies
Section: 80GGC	Contributed amount (Not in cash)	Contribution made to political parties by individuals
Section: 80RRB	Income received / Rs 3,00,000 (w.e.l.)	Income received from royalty or patent

AMOUNT OF EXEMPTION ON HRA :

Whichever is least of the below is exempted on HRA

- (a) Actual HRA received
- (b) Rent Paid (MINUS) 10 % of Salary
- (c) 50% of salary in Metro City & 40% of salary in other cities.

Note : Salary = Basic Pay + DA (Enter)+Commission(Fixed %)

AMOUNT OF EXEMPTION ON EA (only for Government employee) :

Whichever is least of the below is exempted on EA

- (a) Actual EA received
- (b) Notified Limit Rs.5000
- (c) 20% of Basic Salary

Illustration – 2 :

Santosh Karthiq resides in Chennai, gets Rs.3,00,000 p.a. as basic salary,D.A. Forming part of salary for service benefits Rs.40,000 and 2% Commission on turnover achieved by him. (Turnover achieved by him during the relevant period is Rs.3,00,000) He receives Rs.60,000 as H.R.A. Though he pays a rent of Rs.80,000 p.a.

Computation of Taxable H.R.A of Santosh Karthiq of Chennai for A.Y.2023-24

Particulars	Rs.	Rs.
H.R.A Received		60,000
Less: Least of the following is exempted u/s 10		
1. Actual H.R.A Received	60,000	
2. Rent paid – 10% of Salary(80,000 – 346000 x 10%)	45,400	
3. 50% of salary for Metro city or 40% of salary other than metro(3,46,000* x 50%)	1,73,000	45,400
Taxable HRA		14,600
Salary = Basic pay + DA (SB)+ Commission on Turnover		
Salary* = (3,00,000+40,000+6,000) = 346,000		

Illustration – 3 :

Mohini Kanda is an employee of a partnership firm. She submits the following information. Basic salary Rs. 30,000 p.m. DA Rs.8,000p.m. (1/4 of which is part of salary for retirement benefits) Employer's Contribution to provident fund Rs.4,000 p.m.(Mohini Kanda makes an equal contribution) Interest credited at the rate of 15% is Rs.30,000. Commission received Rs.10,000 based on turnover. Fixed commission Rs.3,000 p.m. Bonus Rs.5,000. Children hostel expenditure allowance received for 3 of her children Rs.15,000.

Case: (A) SPF & (C) URPF

Solution :**Computation of Gross salary of Mohini Kanda for the A.Y.2023-24**

Particulars	Rs.	Rs.
Basic Salary		3,60,000
DA (for service benefits) (8,000 x 1/4 x 12)	24,000	
DA (for other) (8,000 x 3/4 x 12)	72,000	96,000
Employer's Contribution to P.F. (4,000 X 12)	48,000	
Less : Exempted	48,000	NIL
Interest credited to P.F	Exempt	
Commission on Turnover		10,000
Fixed Commission (3,000 x 12)		36,000
Bonus		5,000
Hostel Expenditure Allowance	15,000	
Less: Exempted (300 x 12 x 2)	7,200	7,800
Gross Salary		5,14,800

Case : (B) RPF 10. Computation of Gross salary of Mrs. Mohini Kanda for the A.Y.2020-21

Particulars	Rs.	Rs.
Basic Salary		3,60,000
DA (for service benefits) (8,000 x 1/4 x 12)	24,000	
DA (for other) (8,000 x 3/4 x 12)	72,000	96,000
Employer's Contribution to P.F. (4,000 X 12)	48,000	
Less: Exempted (3,60,000+24,000+10,000)x 12/100	47,280	720
Interest on RPF balance at 15% is	30,000	
Less: Exempted (30,000 x 9.5 / 15)	19,000	11,000
Commission on Turnover		10,000
Fixed Commission (3,000 x 12)		36,000
Bonus		5,000
Hostel Expenditure Allowance	15,000	
Less: Exempted (300 x 12 x 2)	7,200	7,800
Gross Salary		5,26,520

Illustration – 4 :

Sport Star Ltd. provided the following perquisites to its employee Srinivasan, for the FY 2022-23.

1) Leased accommodation provided to the employee. Hire Charges INR 50000 pm; recovered from employee INR 20000pm; 2) Accommodation was furnished and the actual hire charges paid by the employer was INR 4050 pm; 3) He was also provided a Hyundai Santro with Chauffeur and a gift Voucher worth INR 9000. Salary for the purposes of valuation of perquisites is INR 25,00,000. Compute the taxable value of the perquisites assuming assessee had not opted for section 115BAC of the Income Tax Act, 1961.

Solution :

Accommodation on lease	Amount (Rs.)	Amount (Rs.)
Salary for the purposes of Valuation of Perquisites	25,00,000	
Actual lease Charges	6,00,000	
15% of the above (Cap)	3,75,000	
Hence, Gross Taxable Value of the Perquisite		3,75,000
Less: Amount recovered from the employee		-2,40,000
Taxable value of unfurnished leased accommodation		1,35,000
Add: Actual hire charges of furniture hired		+48,600
Taxable value of Furnished Accommodation		1,83,600
Car used partly for Official & partly for Personal		
Engine Capacity is within 1.6 (Santro)		
Taxable Value of Perquisite @ 1800 pm		21,600
Chauffeur @ 900 pm		10,800
Taxable value of Motor Car provided		32,400

Note :

1. Refer to the valuation rules for perquisites – taxable value of perquisite for a hired accommodation is the actual hire charges incurred by the employer subject to max. 25% of salary reduced by the amount recovered from the employee.
2. Since the accommodation is furnished, the actual hire charges are added to the above.
3. Gift Vouchers are taxable as perquisites too if received by the employer and more than 5000

Illustration – 5 :

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 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 1.4.2020 to 30.6.2020)		12,000	
Less: Minimum of the following being exempted u/s 10(13A)			
a) Actual Amount Received	12,000		
b) 40% of Salary [$(\text{₹ } 5,000 + \text{₹ } 2,000) * 3$]	8,400		
c) Rent paid – 10% of salary ($\text{₹ } 12,000 - \text{₹ } 2,100$)	9,900	8,400	3,600
House Rent Allowance Received (from 1.7.2020 to 30.9.2020)		12,000	
Less: Minimum of the following being exempted u/s 10(13A)			
a) Actual Amount Received	12,000		
b) 40% of Salary [$(\text{₹ } 6,000 + \text{₹ } 2,000) * 3$]	9,600		
c) Rent paid – 10% of salary ($\text{₹ } 12,000 - \text{₹ } 2,400$)	9,600	9,600	2,400
House Rent Allowance Received (from 1.10.2020 to 31.12.2020)		12,000	
Less: Minimum of the following being exempted u/s 10(13A)			
a) Actual Amount Received	12,000		
b) 50% of Salary [$(\text{₹ } 6,000 + \text{₹ } 2,000) * 3$]	12,000		
c) Rent paid – 10% of salary ($\text{₹ } 12,000 - \text{₹ } 2,400$)	9,600	9,600	9,600
House Rent Allowance Received (from 1.1.2021 to 31.3.2021)			
(Fully taxable as assessee resides in his own house)			12,000
Taxable House Rent Allowance			20,400

Special allowance exempt U/s*10(14)

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

Illustration – 6 :

Nitin is an employee of XYZ Ltd. he was appointed on 1st Mar 2022 at a scale of 50000 – 5000 – 70000. He is paid DA(which forms part of retirement benefits) @ 15% of Basic Pay and Bonus equivalent to 2 month's salary at end of FY. He contributes 18% of his Basic + DA to a recognised provident fund, and the contribution is matched by the employer. He is provided rent free accommodation, hired by the employer, @ 25000 pm. He is also provided the following benefits / amenities :

- a) Medical Treatment of his dependant spouse INR 40000.
- b) Monthly salary to housekeeper INR 4000.
- c) Telephone Allowance INR 1200 pm.
- d) Gift Voucher of INR 4500 on account of his marriage anniversary.
- e) Medical Insurance Premium for Nitin, paid by his employer INR 15000.
- f) Motor Car owned and driven by Nitin, and engine capacity within 1.6 liters; used partly for official and partly for personal purposes. Running & maintenance expenses are borne by the employer INR 36,600.
- g) Lunch during office hours valued at INR 2200.

He was also allotted 2000 sweat equity shares in September 2022. The shares were allotted @ INR 227 per share against the FMV of INR 377 per share as on the date of exercise of the option.

Compute the Salary income chargeable to tax.

Option 1 : Assessee has not opted for Section 115BAC

Option 2 : Assessee has opted for Section 115BAC

Solution :

Option 1 : Assessee has not opted for Section 115BAC (Hindu Undivided Family)

Particulars	Amount	Amount
Basic		6,05,000
DA		90,750
Bonus		1,10,000
Employers' Contribution to Pf > 12%		41,745
Taxable Allowances		
Telephone		14,400
Taxable Perquisites		
Medical Reimbursement (fully Taxable)		40,000
Housekeeper		48,000
Motor Car		15,000
Rent free Accommodation		1,23,023
Sweat equity		3,00,000
Gross Salary		13,87,918
Less: Standard Deduction under section 16(ia)		50,000
Taxable Salary		13,37,918

Note :

- 1) Employer's Contribution to Provident fund in excess of 12% is chargeable to Income Tax.
- 2) Rent free Accommodation is valued as under: (a). Since the accommodation is hired, the actual hire charges subject to a cap of 15% of "salary" is considered; (b). "Salary" for this purpose is Basic + DA + Bonus + all Taxable Allowances = INR 8,20,150.
- 3) Medical Treatment is chargeable to Tax, as no more tax free perquisite.
- 4) Since the value of the gift voucher is below INR 5000, it is not taxable as perquisite.
- 5) Lunch during office hours is also not taxable as perquisite assuming cost of meal upto Rs.50 per meal.
- 6) Medical Insurance Premium paid by the employer on behalf of Nitin is also not taxable as perquisite.
- 7) The motor car is chargeable as under :

If the Car is owned / hired by the employee; expenses met by the employer & is used by the employee partly for official and partly for Personal purposes, the taxable value of the perquisite would be the actual expenditure incurred by the employer as reduced by the taxable value of the perquisite determined basis the engine capacity, i.e., Rs. 36600– Rs. (1800*12) = Rs. 15000.

Option – 2 : Assessee has opted for Section 115BAC (Hindu Undivided Family)

Particulars	Amount
Basic	6,05,000
DA	90,750
Bonus	1,10,000
Employers' Contribution to Pf > 12%	41,745
Taxable Allowances	
Telephone	14,400
Taxable Perquisites	
Medical Reimbursement (fully Taxable)	40,000
Housekeeper	48,000
Motor Car	15,000
Rent free Accommodation	1,23,023
Sweat equity	3,00,000
Meals	2,200
Gross Salary	13,90,118
Less: Standard Deduction under section 16(ia)	Nil
Taxable Salary	13,90,118

Note :

1. Employer's Contribution to Provident fund in excess of 12% is chargeable to Income Tax.
2. Rent free Accommodation is valued as under: a) Since the accommodation is hired, the actual hire charges subject to a cap of 15% of "salary" is considered;b) "Salary" for this purpose is Basic + DA + Bonus + all Taxable Allowances = INR 8,20,150.
3. Medical Treatment is chargeable to Tax, as no more tax free perquisite.
4. Since the value of the gift voucher is below INR 5000, it is not taxable as perquisite.
5. Lunch during office hours is taxable as perquisite.
6. Medical Insurance Premium paid by the employer on behalf of Nitin is also not taxable as perquisite.
7. The motor car is chargeable as under:
If the Car is owned / hired by the employee; expenses met by the employer & is used by the employee partly for official and partly for Personal purposes, the taxable value of the perquisite would be the actual expenditure incurred by the employer as reduced by the taxable value of the perquisites determined basis the engine capacity i.e. INR 36600- INR (1800X12) = INR 15000.
8. Deduction u/s 16 is not allowed

Illustration – 7 :

Mr. Ramamoorthy, an employee of M/s. Gopal Krishnan & Co. of Chennai receives during the previous year ended March 31, 2023 the following payments :

Particulars	Amount
Basic Salary	40,000
Dearness allowance	3,000
Leave Salary	5,400
Professional tax paid by employer	1,000
Fair rent of the flat provided by employer	6,000
Rent paid for furniture	1,000
Rent recovered by employer	3,000
Contribution to Statutory Provident fund	4,000
Employer's contribution to Statutory Provident fund	4,000

Compute his taxable income for the Assessment Year 2023-24.

Option 1 : Assessee has not opted for Section 115BAC

Option 2 : Assessee has opted for Section 115BAC

Solution:**Option – 1: Assessee has not opted for Section 115BAC (HUF)****Computation of taxable income of Mr. Ramamoorthy for the Assessment Year 2023-24**

Particulars		Amount
Basic Pay		40,000
Dearness allowance		3,000
Leave Salary		5,400
Professional tax paid by employer		1,000
Perquisite for house :		
15% of salary (Rs. 40,000 + 3,000 + 5,400)	7,260	
Add: Furniture Rent	1,000	
Less: Rent recovered	-3,000	5,260
		54,660
Less: Standard Deduction u/s 16(ia)		-50,000
Less: Professional Tax u/s 16		-1,000
Gross Total Income		3,660
Less: Deduction under Section 80C		-3,660
Total income		Nil
Total tax payable		Nil

Note : Assumed that dearness allowance forms part of the salary for the purpose of computation of superannuation or retirement benefits.

Option – 2 : Assessee has opted for Section 115BAC**Computation of taxable income of Mr. Ramamoorthy for the Assessment Year 2023-24**

Particulars		Amount
Basic Pay		40,000
Dearness allowance		3,000
Leave Salary		5,400
Professional tax paid by employer		1,000
Perquisite for house :		
15% of salary (Rs. 40,000 + 3,000 + 5,400)	7,260	
Add: Furniture Rent	1,000	
Less: Rent recovered	-3,000	5,260
		54,660
Less: Standard Deduction under section 16(ia)		Nil
Less: Professional Tax u/s 16		Nil
Gross Total Income		54,660
Less: Deduction under Section 80C		Nil
Total income		54,660
Total tax payable		Nil

Note :

- (i) Assumed that dearness allowance forms part of the salary for the purpose of computation of superannuation or retirement benefits.
- (ii) Deduction u/s 16 & 80C is not allowed as the assessee has opted for section 115BAC.

Illustration – 8 :

For the financial year 2022-23, 'Anwar', a Central government officer receives salary of Rs. 77,000 (including dearness allowance of Rs. 42,000) and entertainment allowance of Rs. 18,000. His contribution to provident fund during this period is Rs. 7,200. In addition, he has purchased national Savings Certificates (VIII Issue) for Rs. 6,000. He has been provided with accommodation by the government for which the rent determined is Rs. 375 per month and this is recovered from Anwar's salary. Compute A's tax liability for the assessment year 2023-24 assuming that he has no other income.

Option 1 : Assessee has not opted for Section 115BAC

Option 2 : Assessee has opted for Section 115BAC

Solution :**Option – 1 : Assessee has not opted for Section 115BAC**

Mr. Anwar

Assessment Year: 2023-24

Status: Resident Individual

Statement of Assessable Income

Particulars	Amount	Amount
Salary from Central government		77,000
Entertainment allowance	18,000	
Less: Entertainment Allowance u/s 16(ii) Rs. 5,000 or [1/5th of salary exclusive of any allowance, benefit or perquisite]	5,000	-13,000
Less: Standard Deduction u/s 16(ia)		-50,000
Gross Total Income		14,000
Less: Deduction u/s 80C (7,200 + 6,000)		-13,200
Total Income		800
Tax liability		Nil
Net tax payable		Nil

Option – 2 : Assessee has opted for Section 115BAC

Name of Assessee : Mr. Anwar

Assessment Year : 2022-23

Status : Resident

Individual Statement of assessable income

Particulars	Amount	Amount
Salary from Central government		77,000
Entertainment allowance	18,000	
Less: Entertainment Allowance u/s 16(ii)	Nil	18,000
Gross Total Income		95,000
Less: Deduction u/s 80C		Nil
Total Income		95,000
Tax liability		Nil
Net tax payable		Nil

Illustration – 9 :

Mr. Sunith Chouhan is employed in ABC ltd. getting basic pay Rs. 60,000 p.m. and dearness allowance Rs. 10,000 p.m. (forming part of salary). Employer has paid bonus Rs. 20,000 during the year. Commission was allowed @ 2% of sales turnover of Rs.50,00,000. The employer and employee both are contributing Rs. 11,000 (each) to the recognised provident fund. During the year interest of Rs. 10,000 was credited to the RPF @ 10% p.a.

Compute tax liability of Mr. X for A.Y. 2023-24.

Option 1 : Assessee has not opted for Section 115BAC

Option 2 : Assessee has opted for Section 115BAC

Solution :**Option – 1: Assessee has not opted for Section 115BAC**

Particulars		Amount
Basic Pay (60,000 x 12)		7,20,000
Dearness allowance (10,000 x 12)		1,20,000
Bonus		20,000
Commission (50,00,000 x 2%)		1,00,000
Employer's contribution to RPF >12% Salary		19,200
Interest credited in excess of 9.5% p.a. (10,000 / 10% x 0.5%)		500
Gross Salary		9,79,700
Less: Standard Deduction u/s 16 (ia)		-50,000
Income under the head Salary		9,29,700
Gross Total Income		9,29,700
Less: Deduction u/s 80C		1,32,000
Total Income		7,97,700
Computation of Tax liability:		
Tax on Rs. 7,97,700 at slab rate	72,040	
Add: HEC @ 4%	2,882	
Tax liability (Rounded 74920)		74,920

Option – 2 : Assessee has opted for Section 115BAC

Particulars		Amount
Basic Pay (60,000 x 12)		7,20,000
Dearness allowance (10,000 x 12)		1,20,000
Bonus		20,000
Commission (50,00,000 x 2%)		1,00,000
Employer's contribution to RPF >12% Salary (Note 2)		*19,200
Interest credited in excess of 9.5% p.a. (10,000 / 10% x 0.5%)		500
Gross Salary		9,79,700
Less: Standard Deduction u/s 16 (ia)		Nil
Income under the head Salary		9,79,700
Gross Total Income		9,79,700
Less: Deduction u/s 80C		Nil
Total Income		9,79,700
Computation of Tax liability:		
Tax on Rs. 9,79,700 at slab rate (u/s 115BAC Note;1)	71,955	
Add: HEC @ 4%	2,878	
Tax liability (Rounded 74920)		74,830

Note :

1. Computation of Tax liability Tax on Rs. 9,79,700 at new slab rate [Section 115BAC]

0 to 2,50,000 : Nil

>2,50,000 to 5,00,000 @5%: 12,500

>5,00,000 to 7,50,000 @10% : 25,000

>7,50,000 to 9,79,700 @15% : 34,455

Total = 71955

2. Salary for RPF= 7,20,000 + 1,20,000 + 1,00,000 = 9,40,000 @12% = 1,12,800

Employer's contribution = 11,000 x 12 = 1,32,000

1,32,000 – 1,12,800 = 19,200

Illustration – 10 : Compute taxable amount of commuted value of pension.

If a) He is gets Gratuity b) He is does not gets Gratuity c) He is a Government Employee

Solution :

Mr. Saravanan retired on 31st Dec, 2019 and his pension is fixed at Rs.3,600 p.m. He got 3/4th of pension commuted for which hereceived Rs. 1,80,000 from his employers.

- a) Mr. Saravanan is the non-government employee receives gratuity along with pension, only 1/3 of Commuted value is exempt.

Exempted Value $(1,80,000 \times \frac{4}{3} = 2,40,000 \times \frac{1}{3} = 80,000)$

Taxable value of commuted pension = Rs. 1,80,000 - 80,000 = Rs. 1,00,000

Monthly pension received is taxable. Monthly Pension from 1-1-2020 to 31-3-2020.

Taxable monthly pension is $(3,600 \times \frac{1}{4} \times 3)$ Rs. 2,700

- b)** Mr. Saravanan retired on 31st Dec, 2019 and his pension is fixed at Rs. 3,600 p.m. He got 3/4th of pension commuted for which he received Rs. 1,80,000 from his employers.

Mr. Saravanan is the non-government employee does not receive gratuity along with pension, only 1/2 of Commuted value is exempt.

Exempted Value $(1,80,000 \times \frac{4}{3} = 2,40,000 \times \frac{1}{3} = 80,000)$

Taxable value of commuted pension = Rs. 1,80,000 - 80,000 = Rs. 1,00,000

Monthly pension received is taxable. Monthly Pension from 1-1-2020 to 31-3-2020.

Taxable monthly pension is $(3,600 \times \frac{1}{4} \times 3)$ Rs. 2,700

- c)** Mr. Saravanan retired on 31st Dec, 2019 and his pension is fixed at Rs. 3,600 p.m. He got 3/4th of pension commuted for which he received Rs. 1,80,000 from his employers.

Mr. Saravanan is the Government employee, Commuted value is fully exempted.

Monthly pension received is taxable. Monthly Pension from 1-1-2020 to 31-3-2020.

Taxable monthly pension is $(3,600 \times \frac{1}{4} \times 3)$ Rs. 2,700

Gratuity :

Gratuity is a retirement benefit given by the employer to the employee in consideration of past services. Sec. 10 (10) deals with the exemptions from gratuity income. Such exemption can be claimed by a salaried assessee. Gratuity received by an assessee other than employee shall not be eligible for exemption u/s 10(10). E.g. Gratuity received by an agent of LIC of India is not eligible for exemption u/s 10(10) as agents are not employees of LIC of India.

Treatment :

Case – A : Gratuity received during continuation of service Gratuity received during continuation of service is fully taxable in the hands of all employee (whether Government or non-Government employee).

Case – B : Gratuity received at the time of termination of service by Government employee Gratuity received at the time of termination of service by Government employee is fully exempt from tax u/s 10(10)(i).

Tax point : Government employee, here, includes employee of the Central or the State Government or local authority but does not include employee of statutory corporation.

Case – C : Gratuity received at the time of termination of service by non-government (including foreign government) employee, covered by the Payment of Gratuity Act.

In such case, **minimum** of the following shall be exempted from tax u/s 10(10)(ii):

1. Actual Gratuity received;
2. 20,00,000; or
3. 15 working days salary for every completed year of service
[Arithmetically, $15/26 \times \text{Completed year of service} \times \text{Salary p.m.}$]

Notes :

- a) Completed year of service includes any fraction in excess of 6 months. (e.g. 7 years 9 months will be treated as 8 years; 7 years 5 months will be treated as 7 years and 7 years 6 months will be treated as 7 years).
- b) Salary here means Basic + DA, last drawn

Illustration – 11 :

Ashok, an employee of ABC Ltd., receives Rs.2,05,000 as gratuity under the Payment of Gratuity Act, 1972. He retires on 10th September, 2020 after rendering service for 35 years and 7 months. The last drawn salary was Rs.2,700 per month. Calculate the amount of gratuity chargeable to tax.

Solution :**Computation of taxable gratuity of Mr. Ashok for the A.Y.2021-22**

Particulars	Details	Amount
Gratuity received		2,05,000
Less: Minimum of the following is exempted as per Sec 10(10)(ii):		
a) Actual gratuity received	2,05,000	
b) Statutory Amount	20,00,000	
c) $15/26 \times$ completed year of service \times salary p.m. [$15/26 \times 36 \times 2,700$]	56,077	-56,077
Taxable Gratuity		1,48,923

Case – D : Gratuity received at the time of termination of service by non-government employee (including foreign government employee) not covered under the Payment of Gratuity Act.

Gratuity received at the time of termination of service by non-government employee being not covered under the Payment of Gratuity Act shall be exempted from tax u/s 10(10)(iii) to the extent of lower of the following :

1. Actual Gratuity received;
2. 20,00,000; and
3. $\frac{1}{2} \times$ Completed year of service \times Average Salary p.m.

Notes :

- a) While calculating completed year of service ignore any fraction of the year. (e.g. 7 years 9 months will be treated as 7 years only)
- b) Average Salary here means, Basic+DA# + Commission (being a fixed percentage on turnover) being last 10 months average salary, immediately preceding the month of retirement. (E.g. If an

employee retires on 18/11/2020 then 10 months average salary shall be a period starting from Jan' 2020 and ending on Oct' 2020).

#If DA is not forming a part of retirement benefit then the same shall not be included in salary for above purpose. However, DA itself shall be fully taxable.

Illustration – 12 :

Mr. Old man retired from his job after 29 years 6 months and 15 days of service on 17/12/2020 and received gratuity amounting Rs.4,00,000. His salary at the time of retirement was basic Rs.6,000 p.m., dearness allowance Rs.1,200 p.m., House rent allowance Rs.2,000, Commission on turnover 1%, Commission on profit Rs.5,000. He got an increment on 1/4/2020 of Rs.1,000 p.m. in Basic. Turnover achieved by assessee Rs.1,00,000 p.m. Calculate his taxable gratuity if he is a —

- Government employee Non-Government employee, covered by the Payment of Gratuity Act;
- Non-Government employee not covered by the Payment of Gratuity Act

Solution :

- Government employee : Taxable amount: Nil as per section 10(10)(i).
- Other cases :

Computation of taxable gratuity of Mr. Old man for the A.Y. 2021-22

Particulars	Case(b)		Case(c)	
	Details	Amount	Details	Amount
Gratuity received		4,00,000		4,00,000
Less: Min. of the following is exempted u/s 10(10) whichever is less				
1. Actual gratuity received	4,00,000		4,00,000	
2. Statutory Amount	20,00,000		20,00,000	
3. $15/26$ * completed year of service * salary p.m. [$15/26$ * 30 * $7,200$]	1,24,615	1,24,615		
$1/2$ * completed year of service * salary p.m. [$1/2$ * 29 * $8,000$]			1,16,000	1,16,000
Taxable Gratuity		2,75,385		2,84,000

Workings for case – (b) :

- Completed year of service is 30 years.
- Salary here means (Basic + Dearness Allowance) last drawn. i.e. ($6,000 + 1,200$) = $7,200$

Workings for case – (c) :

1. Completed year of service is 29 years.
2. Salary here means Basic + Dearness Allowance + Commission on turnover, being last 10 months average just preceding the month of retirement, as shown below :

Particulars	1	2	3	4	5	6	7	8	9	10	Total
	Feb, 20	Mar	April	May	June	July	Aug	Sept.	Oct	Nov	
Basic	5,000	5,000	6000	6000	6000	6000	6000	6000	6000	6000	58000
DA	1200	1200	1200	1200	1200	1200	1200	1200	1200	1200	12000
Commission	1000	1000	1000	1000	1000	1000	1000	1000	1000	1000	10000
Total											80000
Average Salary = 80000/10 = 8000											8000

PENSION [SEC.17(1)(ii)] :

Pension means a periodical payment received by an employee after his retirement. On certain occasions, employer allows to withdraw a lump sum amount as the present value of periodical pension. When pension is received periodically by employee, it is known as Uncommuted pension. On the other hand, pension received in lump sum is known as Commuted pension. Such lump sum amount is determined considering factors like the age and health of the recipient, rate of interest, etc.

Case – A : Uncommuted pension is fully taxable in the hands of all employees whether Government or Non-Government employee.

Case – B : Commuted pension received by a Government employee is fully exempt from tax u/s 10(10A)(i).

Note : Government employee here includes employee of the Central or State Government, Local authority as well as employee of Statutory Corporation. Judges of the High Court and the Supreme Court are also entitled to the exemption [Circular No.623 dated 6/1/1992]

Case – C : Commuted pension received by an employee who also received gratuity [Sec.10(10A)(ii)]

One third of total pension (which assessee is normally entitled for) commuted is exempt.

Tax point : It is immaterial whether the employee is covered by the Payment of Gratuity Act or not.

Case – D : Commuted pension received by an employee who does not receive gratuity [Sec.10(10A)(ii)]

One half of total pension (which assessee is normally entitled for) commuted is exempt.

Notes :

- a) Pension received by a widow or legal heir of a deceased employee shall not be taxable as salary but taxable u/s 56 as income from other sources (further refer chapter “Income from other sources”.)

- b) Where commuted pension is taxable, relief u/s 89 is available.
- c) Pension received from United Nations Organisation is not taxable.

Further, pension received by a widow of the United Nation sex-officials from UN Joint Staff Pension Fund is also exempt.

Illustration – 13 :

Mr. Amit has retired from his job on 31/3/2020. From 1/4/2020, he was entitled to a pension of ` 3,000 p.m. On 1/8/2020, he got 80% of his pension commuted and received ` 1,20,000. Compute taxable pension if he is:

Case – a : Government employee;

Case – b : Non-Government employee & not receiving gratuity

Case – c : Non-Government employee (receiving gratuity, but not covered by the Payment of Gratuity Act)

Solution :

Computation of taxable pension of Mr. Amit for the A.Y.2021-22

Particulars	Case a		Case b		Case c	
	Details	Amount	Details	Amount	Details	Amount
Uncommuted Pension						
- 1/4/2020 to 31/7/2020 (` 3,000*4)	12,000		12,000		12,000	
- 1/8/2020 to 31/3/2021 (` 600 * 8)	4,800	16,800	4,800	16,800	4,800	16,800
Commuted Pension	1,20,000		1,20,000		1,20,000	
Fully exempted u/s 10(10A)(i)	1,20,000	Nil				
Exempted u/s 10(10A)(ii)(½ of 1,50,000#)			-75,000	45,000		
Exempted u/s 10(10A)(ii)(1/3 of 1,50,000#)					-50,000	70,000
Taxable Pension		16,800		61,800		86,800

Commuted Amount for 80% of pension = ` 1,20,000. Commuted amount for 100% of pension = 1,50,000

Illustration – 14 :

Mr. Reddy retired from his private company service on 30th Nov, 2019 after rendering 31 years of service. He received Rs.2,00,000 as his gratuity. His pension was fixed at Rs.1,600 p.m. of which 1/2 of the amount commuted for Rs.1,00,000. Compute taxable gratuity and pension (His salary at the time of retirement was Rs.8,500 p.m.)

Solution :

Computation of taxable gratuity :

Gratuity received by Mr. Reddy, an employee does not covered by the payment of gratuity act, 1972 is exempted up to the least of the following:

- A) Gratuity actually received Rs.2,00,000

- B) Rs.20,00,000, being Maximum allowed as exempt
 C) Half of average salary for every year of completed service:

Salary = Basic pay + DA (8,500 X 1/2 X 31) = Rs.1,31,750

Least of the A,B& C is exempt from tax = Rs.1,31,750.

Taxable gratuity is 2,00,000 – 1,31,750 = Rs.68,250

Computation of taxable Pension :

Mr. Reddy is the non-government employee receives gratuity alongwith pension, only 1/3 of Commuted value is exempt.

Exempted Value (1,00,000 X 2/3 = 2,00,000 X 1/3 = Rs.66,667)

Taxable value of commuted pension= Rs.1,00,000-66,667 = Rs.33,333

Monthly pension received is taxable. Monthly Pension from

1-12-2019to 31-3-2020 = 1,600 x 1/2 x 4months = Rs.3,200

Taxable monthly pension is Rs.3,200

Illustration – 14 :

Mr. Solanki was an employee of Uthara Ltd which is not covered by payment of Gratuity Act. The following particulars were furnished for the year ending 31-3-2022

- i. Basic pay Rs.8000 pm
- ii. DA # 3000 pm as per terms of employment
- iii. He retired on 1-1-2022 after completing 32 years of service. He received a pension of Rs. 4000 pm and gratuity of Rs.180000.
- iv. His average monthly salary including D.A. was 11000 for the last 10 months
- v. He also receives Rs.200,000 from an unrecognised P.F

Assuming that salary is due on the last day of each month, compute taxable salary.

Solution :

Particulars	Amount
Basic Pay 8000x9 months (retired on 1-1-22)	72000
DA 3000x9 months	27000
Pension for 3 months x 4000	12000
Gratuity (180000-176000*)	4000
Lump sum of URPH (Half is the employer contribution)	100000
Gross salary	215000
Less: Standard Deductions	50000
Net Salary	165000

Note : Computation of Gratuity*

Least of the following :

- i. $11000 \times \frac{1}{2} \times 32 = 176,000$
- ii. Actual Gratuity Rs. 180,000
- iii. Statutory amount Rs.20,00,000

Illustration – 15 :

Mr. Pillai is working in a Textile Mill in Ahmedabad. The following are his incomes :

1. Basic pay Rs.7,000 p.m.
2. D.A. (half is considered for retirement benefit) Rs.2500 p.m.
3. Entertainment allowances Rs.1500 p.m.
4. Children education allowances (for 1 child) Rs.350 p.m.
5. Provided a rent-free house, the fair rent of which is Rs.48000 (population exceeds 25 lakh). He is also provided with furniture costing Rs.48000 in the house
6. Provided a small car for private use of Mr. Pillai. its maintenance cost is Rs.82,400, depreciation Rs.30000 and driver's salary Rs.5000pm
7. Provided free lunch @ 60 per meal for 250 days
8. Reimbursed Rs.15000 for medical treatment in a private hospital
9. He and the company contributes 14% of salary to a RPF. Compute Salary Income.

Particulars	Amount	Amount
Basic Pay 7000x12months		84000
DA 2500x12 months		30000
Entertainment Allowances 1500x12		18000
Children's education allowances: 350x12	4200	
Less: Exempted	1200	3000
Value of car (82000+30000+60000) for personal use		172000
Lunch Allowances (250x10) (exempted upto Rs.50 a meal)		2500
Medical Reimbursement		15000
Employer's contribution to R.P.F (2% of 84000+15000)		1980
Value of rent-free accommodation *		22800
Gross Salary		349680
Less: Standard Deductions		5000
Net Salary		299,680

Value of House *

Salary for computation of HRA = Basic + Medical Reimbursement + Entertainment Allowances + Education allowances

Income Tax	4.23	Computation of Income ...
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15% of (84000+15000+18000+3000) =	18000
Add : 10% of 48000	4800
Total	22800

Illustration – 16 :

Mr. Atul Krishna is a government employee at Agra. He is living in a furnished bungalow provided by the government having a rent of Rs.1000pm. He is provided with furniture costing Rs.20,000. His basic salary is Rs.60,000 p.m. and DA Rs.16000 p.m. He also got an entertainment allowance of Rs.800 p.m. and CCA of Rs.100 p.m.

Compute his taxable salary if he paid employment tax of Rs.1800 during the year.

Particulars	Amount	Amount
Basic Pay 60000x12months		720000
DA 16000x12 months		192000
Entertainment Allowances 800x12		9600
CCA 100x12		1200
Rent free House (12000+2000)		14000
Gross Salary		9,36,800
Less: Deduction u/s 16		
Standard deduction	50,000	
Entertainment allowances	5000	
Employment tax	1800	56,800
Income from Salary (net salary)		8,80,000

Illustration – 17 :

Mr. Martin is a professor of a college in Bangalore. From the following information, compute his taxable salary

- Basic pay Rs.60,000 pm
- DA under the terms of employment Rs.15,000 pm
- He contributes 10% of Basic pay to R.P.F to which the employer also contributes similar amount
- Education allowance to his 3 children Rs.6000
- Medical allowances Rs.8,000 (actual amount spent Rs,3000)
- Telephone bills paid by employer Rs.6,000
- Salary of sweeper, servant and watchman on a salary of Rs.300 pm per person paid by employer
- Surrender of earned leave Rs.25,000
- LIC premium paid by employer Rs.5,000

- j) Provided a rent-free house at Bangalore (population exceeds 25 lakh) value of furniture provided Rs.2,00,000
- k) Professional tax paid by Prof. Martin Rs.2000

Particulars	Amount	Amount
Basic Pay 60000x12months		720000
DA 15000x12 months		180000
Education Allowances 6000-2400 exempted		3600
Contribution to RPF in excess of 12%		-
Medical Allowances		8000
Telephone bills (exempt)		10,800
Salary of sweeper 12months x 300 x 3persons		25,000
Surrender of earned leave		5,000
LIC Premium		5,000
Rent free House:		
15% of (basic+DA+EA+MA+sweeper) = 7,2000+1,80,000+3,600+8,000+25000) = 9,36,600x15%	1,40,490	
Add: 10% of 2,00,000 furniture	20,000	1,60,490
Gross Salary		11,12,890
Less: Standard Deduction	50,000	
Profession Tax	2,000	52,000
Net Salary		10,60,890

Illustration – 18 :

Mr. Ravi retires from a company on 3rd January, 2022 after serving for 17 years. His basic pay at the time of retirement was Rs.17,600 p.m. and DA of Rs3,200 pm. He received a gratuity of Rs.2,40,000 on retirement.

Compute taxable gratuity if he is covered by payment of gratuity Act.

Solution :

Least of the following is exempt :

- i. $17,600+3,200 \times 15/26 \times 17 = 2,04,000$
- ii. Standard limit Rs. 20,00,000
- iii. Actual Gratuity RS.2,40,000

Hence Rs.2,04,000 is exempted and Rs. 36000 is taxable

4.2. SUMMARY :

Salary comes into existence as a result of employer-employee relationship. In an employer-employee relationship, employee performs his duties and the employer provides him salary. Allowances are part of salary given to employees to meet some

particular requirements such as house rent, conveyance, etc. Allowances may be fully taxable, partially taxable or fully exempt.

4.3 KEYWORDS :

Perquisites :

Perquisites mean any casual emoluments, fees or profit attached to an office in addition to salary or wages. The perquisites may be provided in the form of cash or kind by the employer to his employees.

Pension :

Periodic payment made by an employer to his employee after his retirement is known as Pension.

Unrecognized Provident Funds :

These are the funds which are not recognized by the Commissioner of Income taxes.

Encashment of Earned Leave :

Earned leave is a special privilege given to an employee by the employer.

4.4 SELF ASSESSMENT ILLUSTRATIONS :

Illustration – 1 :

The Following are the particulars of income of Mr. Ramesh (an employee of an Individual) for the previous year ended on 31st March 2023.

- i. Salary Rs.4500p.m
- ii. Bonus equal to two months pay
- iii. Dog allowance – Rs.75p.m
- iv. Special Allowance – Rs.60 p.m.
- v. Employee's contribution to a recognized provident fund @ 15% of salary
- vi. Employer's contribution to the fund @ 15% of the salary
- vii. Interest credited to the provident fund @ 9.5% p.a. is Rs.2,800
- viii. He is provided with free lunch in office. The cost per meals Rs.30
- ix. The employer has given him the use of small car which he uses for personal and official purpose. He meets the expenses for personal purpose from out of his pocket.

Compute the income of Mr. Ramesh from salaries for the A.Y. 2023-2024.

Illustration – 2 :

Mr. Mohan retired on 30th September 2019, after 28 years of service. He is entitled to 1and1/2 month earned leave. During his service he has utilized 16 months EL and the

remaining is encashed for Rs.1,35,000. From the following salary details calculate taxable encashment of earned leave. a) Basic pay Rs.6,200 p.m. up to 31st March 2019 and thereafter increased by Rs.1,500 per month. b) DA- 30% of Basic pay (50% is under terms of appointment) c) Commission under which fixed Rs.4,000 and 3% on Turnover, the turnover being Rs.4,00,000.

Illustration – 3 :

Mr. Das retired on 10-07- 2019, after 18 years of service and received Rs.75,000 as an amount of leave encashment for 15 months. His employer allows 45 days of EL for every one year of service. From the following particulars of his salary income, calculate taxable encashment of earned leave. a) His salary during 2018-19 was Rs.5,000 p.m. and 2019-20 Rs.6,000 p.m. b) Dearness pay Rs.400 per month. c) Commission on turnover at 4%, the turnover being Rs.3,00,000.

Illustration – 4 :

Mr. Sundar gives the following particulars. Calculate taxable encashment of earned leave.

- a) Date of appointment: 01-10-1988.
- b) Date of retirement: 21-07-2019.
- c) Entitlement of earned leave: 2 months per annum.
- d) No. of months EL encashed: 20 months.
- e) No. of months EL applied: 3 months.
- f) Amount of encashment per month: Rs.2,000
- g) Salary during 2018 Rs.4,500 per month and 2019 Rs.5,000 per month.
- h) DA: 50% of Basic pay (25% enters into service benefit)
- i) Commission on turnover- 2%. The turnover being Rs.3,00,000.

Illustratio – 5 :

On 01-08- 2017 an employee starts contributing Rs.800 per month to URPF and interest of Rs.4,500 was credited at 15%. From 01-04- 2018 he starts contributing Rs.800 per month to URPF and interest of Rs.10,500 was credited at 15%. From 01-04- 2019 it was increased to Rs.1,000 per month and interest of Rs.15,000 was credited to URPF at 15%. In all the above years' equal amount was contributed by his employer. On 31-12- 2019, it was transferred to RPF. His salary during 2017-18 Rs.3,000 per month, 2018-19 Rs.4,000 per month, 2019-20 Rs.4,500 per month. Calculate taxable transferred balance.

4.5 SUGGESTED READINGS :

1. R. K. Jain, Nikhil Gupta, Manoj Kumar Agrawal, '*Practical Problems in Income Tax*', Scorer Guru Publications, Agra, 2023.

2. Dr. H. C. Mehrotra, Dr. S. P. Goyal, '*Problems and Solutions in Income Tax - Assessment Year 2022-23*', Sahitya Bhawan Publications, Agra, 2022.
3. Dr. H.C. Mehrotra, Dr. S.P. Goyal, '*Corporate Tax Planning & Management - A.Y 2020-21 & 2021-22*', Sahitya Bhawan Publications, Agra, 2020.

G. David Raju

Lesson – 5

INCOME FROM HOUSE PROPERTY

Objectives :

After studying this unit, you should be able to :

- understand various incomes chargeable under the head house property;
- know the list of exempted income from house property; and
- determine the annual value of house property of different categories;
- understand the deductions available and computation of chargeable income under head of house property.

Structure of the lesson :

- 5.1. Introduction
- 5.2. Objectives of Providing Deductions
- 5.3. Important Points regarding Deductions
- 5.4. General Provisions
- 5.5. Deductions in Respect of Payments
- 5.6. Summary
- 5.7. Keywords
- 5.8. Self Assessment Question
- 5.9. Suggested Readings

5.1 INTRODUCTION :

Income from house property is the second head of income since the omission of the head interest on securities and its transference to the head 'income from other sources' by the Finance Act, 1988. The provisions of Income Tax Act, 1961 regarding computation of taxable income from house property are contained in Sections 23 to 27. The taxable income from house property is not the income actually received as rent but is calculated after making many deductions.

According to Section 22 of Income Tax Act, 1961 the assessee has to pay tax on annual value of the property :

1. There must be building and land appurtenant there to.
2. The assessee must be the owner of the property.

3. The property must not be used by the assessee for his/her own business or profession.

The following points to be noted with regard to income from house property can be calculated :

1. This income is limited to the income from building or land appurtenant, i.e., attached to building only. Buildings includes residential houses, warehouses, any block of bricks or stone work covered by a roof etc.,
2. Annual value is defined under section 23(1). According to this section, the annual value of any property shall be deemed to be the sum for which the property might reasonably be expected to be let-out from year to year subject to deduction of municipal taxes.
3. The assessee should be the owner or deemed owner of the house property.
4. In case of dispute about ownership, the person who receives rent shall be liable to pay the tax till the courts order is obtained.
5. If the actual tenant sub-lets full or part of the hired building to another person it is called sub-letting. Sub-letting is taxable under the head income from other sources. Out of actual rent received, the actual expenses pertaining to sub-let port on the allowed to be deducted.
6. If the property is used for the assessee's own business or profession, the annual value of such property is not taxable under the head income from house property but the gains from business/profession which is carried on in such property is taxable under the head income from business/profession.

Deemed Owner of House Property :

In the following cases the assessee is deemed to be the owner of house property :

- a. An individual who transfers any house property to his or her spouse without adequate consideration or to his minor child not being a married daughter.
- b. The holder of an impartible estate.
- c. A person who takes land on lease and constructs a house upon it.

5.2 INCOME FROM HOUSE PROPERTY EXEMPT FROM TAX :

There are two kinds of exemptions regarding income from house property :

- (1) which is totally exempt; and
- (2) which is partially exempt.

The first means which is neither included in total income nor taxable and the second means which is included in total income for rate purposes but is not taxed.

First Category :

Income house property which is totally exempt :

- i) Buildings situated in the immediate vicinity of agricultural land and which is occupied by the cultivator as a dwelling house or as a store house. It is treated as agriculture income and is fully exempt.
- ii) Any one palace in the occupation of a Ruler.
- iii) House properties belonging to a local authority, scientific research association, University or other recognised educational institution, hospital, or Games or Sports Association and Registered Trade Union.
- iv) Property belonging to an authority constituted under any law for the purpose of marketing of commodities and used for letting of godowns or warehouse for storage of commodities.
- v) House property held by a trust established wholly 'for charitable purposes.
- vi) House property held by a political party.
- vii) House property owned by an assessee and used for his own business or professional purposes.
- viii) Self-occupied houses - The Finance Act, 1986 w.e.f. 1.4.1987 provide that where the property consists of one house or part of a house in the occupation of the owner for his own residence and is not actually let out during any part of previous year, the annual value of such a house shall be taken to be nil.

Second Category :

Income from house property which is partially exempt :

- i) Building belonging to a co-operative society and income derived by it from letting , of godowns or warehouses for storage of commodities.
- ii) Building belonging to a co-operative society, where the gross total income of the society does not exceed Rs. 20,000 and the society is not a housing society or an urban consumer's society or a society carrying on transport business or a society engaged in manufacturing operations with the aid of power.

5.3 SOME IMPORTANT POINTS :

(i) Income from house property situated abroad :

Income from any house property I situated abroad is taxable only in case of an individual. Not ordinary resident and non-resident pay tax on such property only when it is received in India. A resident will pay tax on foreign property as if such property is situated in India.

(ii) Disputed Ownership:

If the title of ownership is disputed in a court of law, the decision as to who is the owner rests with the income-tax department. Generally, the recipient of rental income or the person who is in possession of the property is treated as the owner.

(iii) Composite Rent :

If a building is let out to a person along with other facilities (e.g. electricity, cooler, water pump, water tax, etc.) for a composite rent and if the rent of the building can be separated from the rent of such facilities, the two rents will be separated and that belonging to the building only will be taxed under the head 'House Property' and that which belongs to other facilities will be taxed under the head 'Income from other Sources'. If the composite rent cannot be split up it will not be taxed under the head 'House Property', but under the head 'Other Sources'.

(iv) Property owned by Co-owners :

Where a property is owned by two or more persons jointly and their respective shares are definite and can be ascertained then income from such property shall not be assessed on such persons as association of persons, but the share of each person will be calculated and added to their respective total income.

(v) Income from sub-letting :

This is chargeable under the head other sources as the person sub-letting is not the owner.

5.4 ANNUAL VALUE :

The assessee has to pay tax on the annual value of the house owned by him. Therefore, it is very important to calculate properly the annual value of the property. According to Section 23 of Income Tax Act, 1961, the annual value of a house property shall be :

- a) the sum for which the property might reasonably be expected to let from year to year;
- or

- b) where the property is let and the actual rent received or receivable by the owner in respect thereof is in excess of the reasonable rent, the actual amount of rent received or receivable.

Any taxes levied by the local authorities and borne by the owner should be deducted to calculate the annual value of the property.

The above definition makes it clear that annual value of the any house property is its reasonable rent. But, if the actual rent is higher than the reasonable rent then the actual rent received or receivable will be the annual value. It must be noted here that annual value is not determined by actual or reasonable rent alone. In case the rent of house property is fixed by rent controller under the Rent Control Act. The annual value in such a case cannot exceed the rent fixed by the Rent Controller. In case the actual rent exceeds the rent fixed by the rent controller then the actual rent would be the annual value. From the above discussion it is clear that annual value is determined by taking into account many factors. They are:

- i) **Municipal valuation** fixed by the local authorities on the basis of income earning capacity of the property. It is fixed to calculate the house-tax to be paid by the owners.
- ii) **Actual rent** received or receivable from the tenant.
- iii) **Reasonable rent**, i.e. the rent of similar properties in the same locality, and
- iv) **Standard rent** the rent fixed by the Rent Controller under Rent Control Act. 7 Where the Standard Rent is applicable reasonable rent and municipal value will not be taken into consideration even though they are higher than the standard rent.

5.5 COMPUTATION OF ANNUAL VALUE :

When a person owns a house he may occupy it himself or rent it out. The annual value of house property would be different for the house which is given on rent and which is occupied by the owner for his residential purposes. For the purposes of calculation of annual value house property is divided into the following categories :

- 1) House which is let out
- 2) House which is occupied by the owners for residential purposes

Let us now discuss each one of them in detail :

5.5.1 Let Out House :

The house which is let out is divided into two categories :

- (A) Which is not covered by Rent Control Act.
- (B) Which is covered by Rent Control Act.

(A) Which is not covered by the Rent Control Act :

The actual rental income or the rent at which it might be expected to be let out or the municipal valuation, whichever is to be highest, will be gross annual value. Any municipal taxes or tax levied by any local authority paid and borne by the owner shall be deducted from the gross annual value and the balance left will be the net annual value. The municipal taxes shall be deducted in the year in which they are actually paid, whether for current year only or for the previous year and not on accrual basis.

(B) Which is covered by the Rental Control Act :

In this case standard rent is fixed by the Rent Controller. The annual value will be the actual rent received or standard rent, whichever is higher. It will be gross annual value. From the gross annual value any municipal taxes or tax levied by any local authority and paid and borne by the owner will be deducted and the balance left will be the net annual value.

Note :

Even if the Municipal value or reasonable rent is higher than standard rent or actual rent, they will not be considered in this case.

Statutory Deduction :

New houses or units, whose construction commenced after 1st April, 1961, and which are let out for residential purposes are further entitled to statutory deduction from the annual value determined as above. This deduction is allowable for each independent unit of the house separately, as if each unit is a separate house. Each independent unit is that which has separate municipal number, separate electric and water metres and independent latrine; bathroom, kitchen etc. At present, the deduction is relevant for those houses which are completed after 31st March 1982. This deduction is allowed for a period of 60 months from the date of completion. The rate of deduction is as under :

- i) In respect of any residential unit whose annual value as determined does not exceed Rs. 3,600, the amount of such annual value; and
- ii) In respect of any residential unit whose annual value as determined exceeds Rs. 3,600, an amount of Rs. 3,600.

5.5.2 Self-occupied House :

The owner of house can

- A. occupy the house for full year
- B. occupy the house for a part of the previous year and for some part of the previous year it is let out

- C. occupy a part of the house for full year and a part for the part of the year (is. a part of the house is let out for a part of the previous year).

Let us now see how the, annual value of the house is calculated in the above mentioned three cases.

- A. 1) When the house is self-occupied for the full year The annual value of the house which is occupied by the owner for his residential purposes is nil.
- 2) If a part of the house is self-occupied by the owner for full previous year and a part is let out for full previous year, the annual value shall be determined as under :
- i) From the annual value of the full house the proportionate annual value for self-occupied part for whole year will be deducted;
- ii) The balance left will be the annual value of the let out part for full year.

In case the property consists of more than one house in the occupation of the owner for the purpose of his own residence, the annual value in respect of one such house, which the assessee may choose, shall be taken as Nil. The annual value of the remaining self-occupied houses will be determined as if such houses had been let out. However, in respect these other self-occupied houses, which have been deemed to be let out, the statutory deduction will not be allowed.

- B. If the whole house is self-occupied by the owner for a part of the previous year and the whole house is let out for a part of the previous year, the annual value shall be determined as under :
- i) First of all the annual value of the whole house shall be determined.
- ii) Then the annual value for that period shall be deducted during which the house is self-occupied by the owner. .
- iii) The balance left shall 'be the annual value of the house
- C. If a part of the house is let out for a part of the. previous year or a part of the house property is self-occupied.by the owner for full year and a part is occupied, by the owner for a part of the year (i.e. a part of the house is let out for a part of the previous year), the annual value shall be determined as under :
- i) First of all from the annual value of the full house, the proportionate annual value of the self-occupied part which is self-occupied for full year shall be deducted.
- ii) From the balance the proportionate annual value for the period during which the remaining part was self-occupied shall be deducted.

- iii) The balance left shall be the annual value for let out portion for the let out period.

Note :

If the house is newly constructed and is let out for residential purposes during the year, statutory deduction will be allowed as per rules for five years from the date of construction. Such a deduction will be allowed only when the let out portion is an independent unit.

Self-occupied house remaining vacant :

If the owner for some reason is not able to stay in the house then the annual value of such self-occupied vacant house would be nil provided the house is not let out and no other benefit is derived from it by the owner in the previous year.

5.6 DEDUCTIONS FROM ANNUAL VALUE :

For computing the income chargeable under the head 'Income from House Property', Section 24 provides for the following deductions to be made from the adjusted annual value of house property apart from the deductions regarding local taxes and statutory allowance. They are :

1) Repairs :

- a) Where the property is let to a tenant or is deemed to be let out and the owner has undertaken to bear the cost of repairs a sum equal to 116th of adjusted annual value shall be deducted as Repairs Allowance. It is a statutory allowance which is always allowed irrespective of the fact, whether the actual expenditure on repairs is less than or is more than 116th of annual value, or whether no amount is spent on repairs or even if the house remained vacant throughout the previous year.
- b) Where the property is in the occupation of a tenant who has undertaken to bear the cost of repairs, the repair allowance shall be limited to either :
 - i) the excess of annual value over the amount of rent payable for a year by the tenant; or
 - ii) a sum equal to 116th of the annual value, whichever is less.

Note :

If adjusted annual value is less than or equal to actual rent payable during the year, no deduction is allowed in respect of repairs in that year.

2) Insurance Premium :

Any insurance premium paid on house property against the risk of damage or destruction through any cause, e.g., fire, earthquake, lightening and so on. It is only the actual premium paid that can be claimed as deduction.

3) Annual Charge :

If there is an annual charge on the property it is an allowable deduction; but such charge should be legally enforceable and should neither be created, by the assessee voluntarily nor it should be in the nature of capital charge. Thus a revenue annual charge is allowable as deduction only if it has not been created by the assessee voluntarily. It does not include any tax in respect of the property

4) Ground Rent :

The owner of a building -may be lessee of the land on which the building is erected. Any ground rent payable in respect of the lease of that land is allowable as a deduction on accrual basis. NO deduction is allowed for interest on enhanced ground rent but any additional ground rent paid to regularise the unauthorized, use of building is allowed.

5) Interest on Loan Taken in Respect of House Property :

Interest on loan taken for the purpose of purchasing, constructing, reconstructing or repairing the house property is allowable as a deduction on accrual basis. It is not necessary, for the purpose, that the loan borrowed or the interest payable thereon is secured by a charge on property.

Explanation :

Interest payable in respect of funds borrowed for the acquisition or construction of house property and pertaining to the period prior to the previous year in which such property has been acquired or constructed, shall be deducted in five equal annual installments commencing from the previous year in which the house was acquired or constructed.

6) Land Revenue and Property Tax :

Any sum paid on account of land revenue or any other tax levied by the State Government in respect of the property is deductible.

7) Collection Charges:

Any sum spent to collect the rent from the property, not exceeding 6% of adjusted annual value of the property, is allowed as deduction. It includes (i) legal expenses incurred to collect the rent, (ii) salary paid to an employee to collect the rent, (iii) conveyance charges incurred to collect the rent, (iv) postal charges incurred to collect the rent, (v) bank commission to collect the rent.

8) Vacancy Allowance :

When the property is let and remains vacant during a part of the year, the part of the adjusted annual value which is proportionate to the period during which the property is wholly unoccupied will be deducted as 'vacancy allowance'. Where the property is let out in parts, and any part of it remains vacant for a part of the previous year, that portion of

the adjusted annual value appropriate of any vacant part, which is proportionate to the period during which such part remains vacant will be deducted as 'Vacancy Allowance'. Where the property remains vacant for full year, no vacancy allowance will be available.

9) Unrealised Rent :

If the assessee is unable to recover the entire amount of rent due from his tenant .in respect of house property let out to him, the unrealised amount of rent shall be ,deducted from the adjusted annual value of that house, provided that it fulfills the following conditions:

- i) the tenancy is bonafide;
- ii) the defaulting tenant has vacated or legal 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;
- iv) the assessee has taken all reasonable steps of instituting legal proceedings for the recovery of the unpaid rent or satisfies the Assessing Officer that legal proceedings would be useless; and
- v) the annual value of the property to which the unpaid rent relates has been included in the assessed income of the previous year during which the rent was due and tax has been duly paid on such assessed income. This is subject to the limit that deduction to be allowed on this account shall not exceed the income under the head 'Income from House Property' included in the total income as computed without making this deduction. Unrealised rent would be deductible from the income from house property in each assessment year till such deductible is exhausted. From the assessment year 1987-88 no deduction will be allowed in respect of self-occupied property where annual value is nil or in respect of the property which cannot be occupied and whose annual value is nil. However, this prohibition will not hit the deduction of interest on capital borrowed for construction, repairs, etc. of self-occupied property if the amount of interest does not exceed Rs. 5,000.

5.7 COMPUTATION OF TAXABLE INCOME FROM HOUSE PROPERTY :

Computation of income from house property is done in the following proforma :

Fair Rental Value of the house :		XXXX
(Actual rent or Municipal value, whichever is higher, or if Rent Control Act is applicable on the house, Standard Rent or Actual Rent, which is higher)		
Less: i) Local Taxes paid by the owner	XX	
ii) Cost of other facilities provided by the owner to the tenant, such as lift, chowkidar, etc.	XX	XXX
Annual Value		
Less: Statutory Deduction for 5 years (In case of newly built house after 31.3.1982 and let out for residential purposes)		XXXX
Adjusted Annual Value		XXX
Less: Deductions :		
i) Repairs Allowance	XX	
ii) Insurance Premium Paid	XX	
iii) Annual Charge	XX	
iv) Ground Rent	XX	
v) Interest on Loan taken in respect of house property	XX	
vi) Land Revende paid	XX	
vii) Collection Charges paid (restricted to 6% of A.A.V.)	XX	
viii) Vacancy Allowance	XX	
ix) Unrealised Rent	XX	XXX
Taxable Income from House Property		XXXX

5.8 SUMMARY :

Income from house property is second major head of income. Income from house property is the annual value of any property which consists of building and land apartment thereto, is owned by the assessee and is not used for assessee's business or profession.

Annual value of the propriety is not the rent received but the reasonable rent, but where actual rent is higher than the reasonable rent the annual value is the actual rent received as reduced by the municipal taxes borne by the owner of the house.

For the purposes of computation of annual value the house property is divided into two:

- i) Let out house

ii) Self-occupied house.

A house which is let out can either be under Rent Control Act or not. When it is not under Rent Control Act the annual value is actual rent, reasonable rent or municipal value whichever is higher as reduced by municipal taxes paid by the owner. When it is under Rent Control Act the annual value is actual rent or standard rent (as fixed by rent controller) whichever is higher as reduced by municipal taxes paid by the owner.

A self-occupied house can be divided into :

- i) Self-occupied house for full year-annual value is nil.
- ii) Part of the house is self-occupied and a part is let out for full year-annual value is calculated as :

Annual value of the full house for full year

Less : annual value of self-occupied house for full year.

- iii) Full house self-occupied for a part of year and let out for the remaining part of the year. Then, annual value is calculated as follows:

Annual value of full house for full year.

Less : annual value of full house for the period for which it is self-occupied.

- iv) A part of the house is let out for a part of the previous year, then the annual, value is :

Annual value of full house for full year

Less : proportionate annual value of self occupied part for full year

Less : proportionate annual value of self-occupied portion for part of these year.

Statutory deduction is allowed on all the houses newly constructed for five years from the date of completion @ Rs. 3,600 on each independent unit let out. Annual Value as reduced by statutory deduction is called adjusted annual value. Certain deductions are allowed from adjusted annual value to compute income from house property.

5.9 KEY WORDS :

Annual Value :

Annual value of a house property is reasonable rent or actual rent (if let out) whichever is higher as reduced by municipal taxes borne by the owner.

Composite Rent :

When the building is let out along with certain facilities e.g. lift. Electricity, etc. then the rent includes the rent for the house and these facilities. Such a rent is called composite rent.

Ground Rent :

Rent paid by the lessee on the land on which his building is erected:

Municipal Value :

Value of the property fixed by local authorities on the basis of its income earning capacity.

Reasonable Rent :

Rent of similar properties in the same locality.

Standard Rent :

Rent fixed by the Rent Controller under Rent Control Act.

Statutory Deduction :

Deduction available to newly constructed houses for five years from the date of completion.

Unrealised Rent:

Rent not recoverable by the owner.

5.10 SELF ASSESSMENT QUESTIONS :

- 1) Define annual value and state the deductions that are allowed from the annual value in computing the income from house property.
- 2) What are the various deductions allowed from Annual Value?
- 3) What are some important points to be followed while determination of annual value?
- 4) Write short notes :
 - a) Vacancy Allowance
 - b) Unrealised Rent
 - c) Repair Allowance
 - d) Income from House Property in foreign country
 - e) Standard Rent.
- 5) How would you determine the annual value of house property, which is self-occupied for a part of the year only and let out for the remaining part?

5.11 SUGGESTED READINGS :

1. R. K. Jain, Nikhil Gupta, Manoj Kumar Agrawal, Sanjeev S. Thakur, '*Practical Problems in Income Tax*', Scorer Guru Publications, Agra, 2023.
2. Dr. H. C. Mehrotra, Dr. S. P. Goyal, '*Problems and Solutions in Income Tax - Assessment Year 2022-23*', Sahitya Bhawan Publications, Agra, 2022.

3. Dr. H.C. Mehrotra, Dr. S.P. Goyal, '*Corporate Tax Planning & Management A.Y 2020-21 & 2021-22*', Sahitya Bhawan Publications, Agra, 2020.

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Lesson – 6

COMPUTATION OF INCOME FROM HOUSE PROPERTY (Problems)

Objectives :

- To acquire knowledge about Computation of Income from House Property and allowable deductions.

Structure of the lesson :

- 6.1. Solved Illustrations on Computation of Income from House Property
- 6.2. Summary
- 6.3. Keywords
- 6.4. Self Assessment Illustrations
- 6.5. Suggested Readings

6.1 Solved Illustrations on Computation of Income from House Property :

Illustration – 1 :

Mr. X is the owner of the following house Property in Mysore. Particulars in respect of the which for the year ending 31- 03-2022 are as follows. Compute his income for the House Property the Assess year.

Particulars	House – I	House – II	House - III
Annual Rent for 12 months	24,000	18,000	Nil
Standard Rent	18,000	12,000	Nil
Municipal Value	16,000	14000	35600
Total Municipal Tax	1600	1400	3560
Municipal Tax paid by X	1600	700	3560
Municipal Tax paid by tenant	Nil	700	Nil
Repairs	1000	500	2000
Vacancy Period	2months	Nil	Nil
Interest on loan for repairing House	800	600	2000
Unrealized Rent allowed in the A.Y 23-24	4000	Nil	Nil

Solution :

Computation of Income from House Property

PARTICULARS	House -I	House - II	House - III
Municipal Rent (or) Fair Rental Value (Which ever is Higher)	16,000 ----	14,000 ----	Nil ----
Notional Rent	16,000	14,000	Nil
Notional Rent (or) Standard Rent (Which ever is less)	16,000 18,000	14,000 12,000	Nil Nil
Expected Rent	<hr/> 16,000	<hr/> 12,000	<hr/> Nil
Expected Rent (or) Annual Rent (Which ever is higher)	16,000 24,000	12,000 18,000	Nil Nil
Gross Annual Rent	<hr/> 24,000	<hr/> 18,000	<hr/> Nil
Less: Vacancy Loss(24,000x2/12)	4,000	---	Nil
Gross Annual Value:	<hr/> 20,000	<hr/> 18,000	<hr/> Nil
Less: Municipal Tax Paid by the owner	1,600	700	Nil
Net Annual Value	<hr/> 18,400	<hr/> 17,300	<hr/> Nil
Deductions u/s 24:	5,520	5,190	Nil
1.) 30% of NAV	800	600	2,000
2.) Interest on Loan	<hr/> 12,080	<hr/> 11,510	<hr/> -2,000
Add: Unrelised Rent recovered	4,000	----	----
Income From House Property	<hr/> 16,080	<hr/> 11,510	<hr/> -2,000

Total Income from House Property

$$16,080 + 11,510 - 2,000 = 25,590.$$

Illustration – 2 :

Compute Income from House Property own by Mr. Amit for A.Y. 2023 – 2024. The following information are as follows :

House – I :

Mysore : Municipal Valuation Rs. 10,000. Municipal taxes paid to 10% of Municipal Value. The house is used by Amit for his residence.

House – II :

Tumkur : Annual Rent Rs. 37,200. Municipal taxes paid Rs. 8,800. Ground Rent payable Rs. 60. Interest on money borrowed for construction Rs. 5,000. Unrealized Rent admissible according to provision of act Rs. 10,000.

House – III :

Ramnagar : Municipal valuation Rs. 6,000. It is let out for Rs. 400 per month. 1/3 portion of this house self occupied by him for his residence. Rent received is for the remain ing 2/3 portion. Municipal taxes paid to 10% of municipal value. Repairs and Annual charge Rs. 1,000.

House – IV :

Mumbai : Actual Rent received Rs. 4,500. Total Municipal taxes Rs.630 out of which Amit paid Rs.420. Interest on loan for renewing the house Rs. 150. Unrealized rent allowed in A.Y. 2023 – 24. Recovered during the year Rs. 2,000.

Computation of Income from House Property

Particulars	House – I (Self-Occupied)	House – II (Let out)	House – III 1/3 deemed to be let out	House – IV (Let out)
Gross Annual Value	Nil	37,200	6,000	4,500
Less: Municipal Taxes paid by the Owner	Nil	8,800	600	420
Unrealised Rent	Nil	10,000	Nil	Nil
Net Annual Value	Nil	18,400	5,400	4,080
Less: Deductions U/S 24:				
1. 30% on NAV	Nil	5,520	1,620	1,224
2. Interest	Nil	5,000	Nil	150
	Nil	7,880	3,780	2,706
Add: Unrealised Rent	Nil	Nil	Nil	2,000
Income from House Property	Nil	7,880	3,780	4,706

- Note :**
- Gross Annual Value of House III has been determined as follows:
Municipal Value or expected rent (w.e.h)
Actual Rent Rs. 4,800 or Municipal Value Rs. Rs. 6,000 (w.e.h)
 - Other expenses are not allowed.

Illustration – 3 :

Mr. Praveen is the Owner of three Houses. The particulars are as follows :

PARTICULARS	House - A	House – B	House - B
Annual fair rent	40,000	35,000	50,000
Municipal Value			
Standard rEnt	50,000	40,000	50,000
Let out (per month)	45,000	42,000	55,000
Purpose	3,000	2,500	---
	let out	let out	Self occupied
Repairs			
Collection charges	2,000	---	5,000
Interest on loan	3000	1000	---
	15,000	5,000	2,000

Municipal tax is 10% of municipal value. Municipal tax of house A was paid by tenant, But municipal tax of house B was not paid till 31.03.23 municipal tax of house C was Paid by owner. House A remained vacant for 4 months. Compute income from house Property for A.Y.2023-24.

Solution :**Computation of gross total income**

Assessee: Mr. Praveen	Previous Year : 2022-23
Status: Resident	Assessment Year: 2023-24
House-A: Let out Residential	Rs.
Municipal Rental Value	50,000
Or	
Fair Rental Value	40,000
Notional Rent (whichever is higher)	50,000
Or	
Standard Rent	45,000
Expected Rent (whichever is lower)	45,000
Or	
Actual Rent (Rs.3,000 X 12)	36,000
Gross Annual Value before Vacancy period (whichever is higher)	45,000
Less: Vacancy Period (Rs.3,000 X 4)	12,000
Municipal Taxes paid	---

Net Annual Value (NAV)	33,000
Less: Standard Deduction U/s – 24	
(i) 30% of NAV	9,900
(ii) Interest on Loan	15,000
Taxable Income from House-A	8,100

House-B: Let out	Rs.
Municipal Rental Value	40,000
Or	
Fair Rental Value	35,000
Notional Rent (whichever is higher)	40,000
Or	
Standard Rent	42,000
Expected Rent (whichever is lower)	40,000
Or	
Actual Rent (Rs.2,500 X 12)	30,000
Gross Annual Value (whichever is higher)	40,000
Less: Municipal Taxes paid	---
Net Annual Value (NAV)	40,000
Less: Standard Deduction U/s – 24	
(i) 30% of NAV	12,000
(ii) Interest on Loan	5,000
Taxable Income from House-B	23,000

House-C: Self Occupied	Rs.
Gross Annual Value	Nil
Less: Municipal Taxes paid	Nil
Net Annual Value (NAV)	Nil
Less: Standard Deduction U/s – 24	
(i) 30% of NAV	Nil
(ii) Interest on Loan	2,000
Loss from House-C	- 2,000

Computation of Income from House Property	Rs.
House-A	8,100
House-B	23,000
House-C	-2,000
Taxable Income from House Property	29,100

Illustration – 4 :

Sri Ramappa (Resident) owns four houses (House – 2 and 4 are self occupied for residence, House- is used own business and House -1 is let out) and furnishes the following information for the financial year 2016-17. Compute his income from House property for the relevant A.Y.2017-18.

Particulars	House-1	House-2	House-3	House-4
Municipal valuation	49,000	28,000	87,000	90,000
Fair rent	42,000	25,000	80,000	1,05,000
Standard rent	38,000	15,000	75,000	90,000
Rent (property is let out Throughout the previous year)	42,000	-	-	-
Unrealized rent	3,500	-	-	-
Municipal taxes:				
Paid by Ramappa	-	500	7,000	90,000
Paid by tenant	5,000	-	-	-
Repairs	2,500	4,500	2,250	3,000
Land revenue to State Govt.	1,000	500	1,200	1,300
Education Cess to Govt.	250	200	300	350
Water & Health Cess to Municipality paid by Ramappa		100	400	800
Date of completion of Construction	31-5-2020	31-5-20	31-5-20	1-4-20

Property - 1 remained vacant for two months (March 16,2022to May 15, 2022). Mr. Ramappa borrows Rs.50,000/-, Rs.75,000/-, Rs.1,00,000/- for the construction of House-1, House-2 and House-4 respectively on 15th June 2012 at the rate of 12% p. a. However, he makes repayment of loan amount of Rs.50,000/-, Rs.25,000/- in respect of House-1 and house-2 respectively on December 31, 2022.

Solution :

Computation of Taxable Income from House Property

PARTICULARS	HOUSE - I	HOUSE - II	HOUSE - III
Nature Occupation	L.O.P	D,L,O,P	S.O.P
Gross Annual Value	36,750	15,000	Nil
Less: Municipal Taxes Paid by the Owner(500+100)	---	600	----
	<u>36,750</u>	<u>14,400</u>	<u>Nil</u>
Net Annual Value			
Less: Standard Deduction:			
30% of NAV	11,025	4,320	Nil
Interest on Loan	1,850	9,075	16,300
Income /loss from House Property	<u>23,875</u>	<u>1,005</u>	<u>(16,300)</u>

Calculation of Gross Annual Value :

PARTICULARS	House - I	House - II	House - III
Fair Rental Value	42,000	25,000	1,0,5000
Or			
Municipal Value	49,000	28,000	90,000
Notional Rent	49,000	28,000	1,05,000
Notional Rent	49,000	28,000	1,05,000
Or			
Standard Rent	38,200	15,000	90,000
Expected Rent	38,200	15,000	90,000
Expected Rent	38,200	15,000	90,000
or			
Actual Rent (42,000-3,500)	38,500		
Unrealised Rent	38,500	15,000	90,000
Balance	1,750	----	-----
Less: Loss of Vacancy	36,750	15,000	90,000
Gross Annual Value			

Illustration - 5 :

Mr. Prem owns a house in Madras. During the previous year 2022-23, 2/3rd portion of the house was self-occupied and 1/3rd portion was let out for residential purposes at a rent of Rs.8,000 p.m. Municipal value of the property is Rs.3,00,000 p.a., fair rent is Rs.2,70,000 p.a. and standard rent is Rs.3,30,000 p.a. He paid municipal taxes @ 10% of municipal value during the year. A loan of Rs.25,00,000 was taken by him during the year 2018 for acquiring the property. Interest on loan paid during the previous year 2022-23 was Rs.1,20,000. Compute Prem's income from house property for the A.Y. 2023-24.

There are two units of the house. Unit I with 2/3rd area is used by Prem for self- occupation throughout the year and no benefit is derived from that unit, hence it will be treated as self-occupied and its annual value will be Nil. Unit 2 with 1/3rd area is let-out throughout the year and its annual value has to be determined as per section 23(1).

Solution :**Computation of income from house property of Mr. Prem for A.Y. 2023-24**

Particulars	Rs.	Rs.
Unit I (2/3rd area – self-occupied)		
Annual Value		Nil
Less: Deduction under section 24(b) [2/3 rd of Rs.1,20,000]		80,000
Income from Unit I (self-occupied)		-80,000

Unit II (1/3rd area – let out)			
Computation of GAV			
Step-I	Computer Expected Rent (ER)		
	ER = Higher of MV and FR, restricted to SR. However, in this case, SR of Rs.1,10,000 (1/3 rd of Rs.3,30,000) is more than the higher of MV of Rs.1,00,000 (1/3 rd of Rs.3,00,000) and FR of Rs.90,000 (1/3 rd of Rs.2,70,000). Hence the higher of MV and FR is the ER. In this case, it is the MV.	1,00,000	
Step-2	Compute actual rent received/receivable [Rs.8,000×12 = Rs.96,000]	96,000	
Step-3	Compare ER and actual rent received/receivable		
Step-4	GAV is the higher of ER and actual rent received/receivable i.e. higher of Rs.1,00,000 and Rs.96,000	1,00,000	
Gross Annual Value (GAV)			1,00,000
Less: Municipal taxes paid by the owner during the previous year relating to let-out portion 1/3 rd of (10% of Rs.3,00,000) = Rs. 30,000/3 = Rs. 10,000			10,000
Net Annual Value (NAV)			90,000
Less:	Deductions U/2-24		
	(i) 30% of NAV = 30% of Rs.90,000	27,000	
	(ii) Interest paid on borrowed capital (relating to let out portion) 1/3 rd of INR 1,20,000	40,000	67,000
Income from Unit II (let-out)			23,000

Loss under head “Income from house property” = -Rs. (80,000) + Rs.23,000 = -Rs. 57,000.

6.2 SUMMARY :

Income is taxable under the head ‘house property’ if it arises from a property consisting of any building or lands appurtenant thereto. For computation of income under this head, a house property is classified into three categories – let-out, self-occupied and deemed let-out house property.

The income from a house property is computed on basis of its annual value. Various factors such as municipal valuation, fair rent, standard rent and actual rent are considered to arrive at annual value. Even if a property is not actually let-out during the year, annual value of a property is computed on notional basis and, accordingly, charged to tax. However, if property is self-occupied or cannot be occupied by the owner due to his employment,

business or profession at any other place, then the annual value of any two of such properties is taken as 'nil'.

Chargeability of Income: Any income is taxable under the head 'Income from house property' if following conditions are satisfied.

- *Building and Land Appurtenant thereto*
- *Ownership of Property*
- *Use of property*

For computation of income from house property, a house property has to be classified into following categories:

- (a) Let-out;
- (b) Self-occupied; and
- (c) Deemed let-out.

6.3 KEYWORDS :

Gross Annual Value (GAV) of the property :

The gross annual value of a self-occupied house is zero. For a let out property, it is the rent collected for a house on rent.

Net Annual Value (NAV) :

Net Annual Value = Gross Annual Value – Property Tax.

Unrealized Rent :

The unrealized rent is deducted from the actual rent receivable from the property before computing income from that property, subject to fulfilment of conditions prescribed under Rule 4 of the Income Tax Rules, 1962.

Municipal Taxes :

Municipal taxes including service-taxes levied by any local authority in respect of house property is allowed as deduction: a) Taxes are borne by the owner; and b) Taxes are actually paid by tenant during the year.

6.4 SELF ASSESSMENT ILLUSTRATIONS :

Illustration – 1 :

Mr. Ashok is the owner of a house (not covered under Rent Control Act) which is let out at Rs. 1,500 per month. Municipal taxes of the house are Rs. 1,200 (being 10% of the municipal value) out of which Rs. 700 are paid by the tenant. The reasonable rent is Rs. 10,000 per annum. What will be annual value of the house?

Illustration – 2 :

Mr. X is the owner of two houses (covered under the Rent Control Act) which are let at Rs. 1,000 p.m. and Rs. 1,500 p.m. Municipal taxes on these houses are paid by the owner which amount to Rs. 800 and Rs. 1,000 respectively (being 10% of municipal valuation). The Standard Rents fixed under the Rent Control Act are Rs. 14,000 and Rs. 16,000 per annual respectively. Fair rent of these two houses is Rs. 13,000 and Rs. 14,000 respectively. What will be their Annual Value?

Illustration – 3 :

Determine the Annual Value of house of Mr. Parmod for the A.Y. 2023-24 Municipal value Rs. 70,000 House let-out @Rs. 8,000 p.m. Municipal tax paid by landlord Rs. 7,000 (10% of M.V.) Fair rent Rs. 80,000 House remained vacant for 2 months

Illustration – 4 :

Determine the annual value of house of Mr. Subhash for the A.Y. 2022-24.

	Rs.
Municipal value	1,50,000
Fair rent	1, 70,000
Actual rent per month	15,000
Municipal tax paid by landlord 10% of Municipal Value	
Unrealised rent	25,000

Illustration – 5 :

Determine the annual value of house of Mr. Varun for the A.Y. 2023-24.

	Rs.
Municipal value	2,00,000
Fair rent	1,80,000
Actual rent per month	25,000
Municipal tax paid by landlord	20,000
Unrealised rent	40,000

House remained vacant for two months during the P.Y.

Illustration – 6 :

From the following information of Mr. A, compute the adjusted annual value of the let out period of the house for the Assessment Year 2023-24.

Municipal value Rs.20,000
Municipal tax paid Rs.4,000

House was self-occupied for first six months and for the remaining six months it was let out at the rate of Rs. 2,000 p.m.

Illustration – 7 :

Mr. Ajay Kumar has a house property in Allahabad whose Municipal Valuation is Rs 2,00,000. Its fair rental value is Rs.2,40,000. This property was self-occupied by Mr. Ajay Kumar from 01-04-2022 to 31-07-2022 w.e.f. 1-08-2022; it was let out at Rs 14,500 per month. Compute the annual value of the house property for the AY 2023-24; if Mr. Ajay Kumar has paid the municipal taxes Rs 20,000 on 28-02-2023. These taxes include Rs 5,000 of P.Y. immediately preceding the P.Y.

Illustration – 8 :

Jayashree owns five houses in Chennai, all of which are let-out. Compute the GAV of each house from the information given below :

Particulars	House-I (Rs.)	House-II (Rs.)	House-III (Rs.)	House-IV (Rs.)	House-V (Rs.)
Municipal Value	80,000	55,000	65,000	24,000	80,000
Fair Rent	90,000	60,000	65,000	25,000	75,000
Standard Rent	N.A.	75,000	58,000	N.A.	78,000
Actual Rent Received / Receivable	72,000	72,000	60,000	30,000	72,000

6.5 SUGGESTED READINGS :

1. R. K. Jain, Nikhil Gupta, Manoj Kumar Agrawal, '*Practical Problems in Income Tax*', Scorer Guru Publications, Agra, 2023.
2. Dr. H. C. Mehrotra, Dr. S. P. Goyal, '*Problems and Solutions in Income Tax - Assessment Year 2022-23*', Sahitya Bhawan Publications, Agra, 2022.
3. Dr. H.C. Mehrotra, Dr. S.P. Goyal, '*Corporate Tax Planning & Management - A.Y 2020-21 & 2021-22*', Sahitya Bhawan Publications, Agra, 2020.
4. J.C. Varshney & Nikhil Gupta, "Corporate Tax Planning", SBPD Publication, Agra, 2022.

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Lesson – 7

INCOME FROM CAPITAL GAINS

Objectives :

The objectives of the lesson are :

- To understand the scope of income chargeable under this head;
- To know the provision section 2 (42 A), relating to the period of holding, for classification of capital asset as short- term capital asset and long term capital asset ;
- To describes the capital gains on transfer of depreciable assets
- To understand the cost of acquisition / improvement and indexed cost of acquisition for the purpose of computing the capital gains; and
- To acquaint the exemptions in respect of certain capital gains.

Structure of the lesson :

- 7.1 Introduction
- 7.2 Basis of Charge
- 7.3 Meaning of Capital Assets
- 7.4 Types of Capital Assets
- 7.5 Transfer of a Capital Asset
- 7.6 Scope and Year of Chargeability
- 7.7 Capital Gains on Distribution of Assets by Companies in Liquidation
- 7.8 Deemed Capital Gain
- 7.9 Method of Computing Capital Gain
- 7.10 Exemptions in Respect of Certain Capital Gains
- 7.11 Summary
- 7.12 Key Words
- 7.13 Self Assessment Questions
- 7.14 Suggested Readings

7.1 INTRODUCTION :

Rights and Powers of an Auditor –

An auditor must have certain powers to perform his duties honestly and successfully. The conferred rights and powers of the auditor cannot be restricted or curtailed by the Articles of Association of the Company or by the Board.

This is the fourth head of income chargeable to tax as given in section 14. First of all this income was made chargeable to tax in 1947 and contained the transfer made up and on 31st March 1948. This change was abolished from 1.4.1948 onward but it was received from the assessment year 1957-58 and income accruing from all transfers effected after 31st March 1956 was made chargeable to tax under this head.

Capital gain is the profit one earns on the sale of an asset like stocks, bonds or real estate. It results in capital gain when the selling price of an asset exceeds its purchase price. It is the difference between the selling price (higher) and cost price (lower) of the asset. Capital loss arises when the cost price is higher than the selling price.

7.2 BASIS OF CHARGE (SECTION 45) :

U/s 45 (1) any profits or gains arising from the transfer of a capital assets effected in the previous year shall, save as otherwise provided in section 54, be chargeable to income-tax under the head 'capital gains' and shall be deemed to be the income of the previous year in which the transfer took place.

The above definition can be split into two parts :

- (a) Income arising from the transfer of a capital assets
- (b) Effected in the previous year

And it is essential to study both the parts in detail.

7.3 MEANING OF CAPITAL ASSETS :

The tax is to be levied on any profit or gain occurring on the transfer of a capital assets. Section 2 (14) defines capital assets as "property of any kind held by assessee whether or not connected with his business or profession".

This definition has a very wide coverage as it includes all type of properties, whether movable or immovable, tangible or intangible, fixed or floating. Such assets may represent not only actual ownership but also any right in relation on any property which is capital of being transferred. The goodwill, the lease-hold rights, rights to subscribe for shares and share of partnership etc. are also considered as capital assets for the purpose of this head. In case a person transfers his tenancy rights to another person, it has been held that it is a self-generating assets and is not eligible to tax under capital gains. (C.I.T. v. B.C. Srinivasa shetty (S.C.)) and C.I.T. v. m[₹] Shrinbhai p. Pandale ((Bombay)). With effect from 1.4.1973 jewellery is also include in the term 'capital assets'. Even a license obtained by the assessee from the Government to start some manufacturing activity shall be included in this term.

What is not included in capital asset? Under Section 2(14) following assets have been specially excluded from the scope of the definition of capital assets:

- i. **Stock-in trade** : Any stock-in-trade consumable stores or raw materials held for the purpose of the business or profession of the assessee
- ii. **Personal effects** : personal effects (movable property) including wearing apparel,

motor car, electrical appliances, refrigerator, furniture etc.; ornaments excluding jewellery held for personal use by the assessee or any other member of his family dependent upon him.

With effect from assessment year 2007-08 personal effects like archaeological collections, drawings, paintings, sculptures or any other work of art has been excluded from the definition of a capital asset. Thus from assessment year 2008-09, capital gain will be calculated as and when the above mentioned personal effects are transferred.

Explanation : The Capital Gain on transfer of jewellery is fully taxable and such it is necessary to understand the meaning of term 'jewellery'. According to explanation attached to section 2(14) (ii) the term "jewellery" includes:

- a) Ornaments made of gold, silver, platinum or any other precious metal or any alloy containing one or more of such precious metals whether or not containing any precious or semi-precious stone and whether or not worked or sewn into any wearing apparel;
 - b) Precious or semi-precious stones, whether or not set in any furniture, utensil or other article or worked or sewn into any wearing apparel.
- iii. **Rural Agricultural Land :** Agricultural Land in rural India-but the land should not be situated within the limits of any municipality or cantonment board having a population of 10,000 or more or situated in areas within distance not exceeding 8 kms from the local limits, if such areas are notified by the central Government for the urbanization or other relevant considerations.
 - iv. **Specified Gold Bonds :** 6% gold bonds 1977 or 7% gold bonds 1980 or National Defense Gold Bonds, 1980 issued by the Central Government.
 - v. **Special Bearer Bonds:** 1991 issued by Central Government
 - vi. **Gold Deposits Bonds:** issued under the Gold Deposits Scheme, 1999 or deposit certificates issued under the Gold Monetisation Scheme, 2015 and gold Monetisation Scheme, 2018 notified by the Central Government.

7.4 TYPES OF CAPITAL ASSETS AND GAINS :

For computing capital gains, assets have been divided into two categories:

(i) Short-term capital assets [Section 2 (42-A)] : Short-term capital assets that which is held by an assessee for not more than 36 months immediately preceding the date of its transfer.

In the case of shares held in a company the period has been reduced to 12 months with effect from 1-4-88 i.e. assessment year 1988-89.

With effect from assessment year 1995-96, the securities listed is any recognised

stock exchange, units of U.T.I. and units of Mutual Funds shall be treated as Long Term capital assets if held for 12 months or more.

In case an assessee subscribes to right issue himself, or subscription is made by renounce the period shall be counted from the date of allotment of such financial asset.

In case subscription is made against the rights being renounced in favour of any other person the period shall be counted from the date on which offer is made by the company or financial institution.

Any gain or loss accruing to the assessee on such assets shall be known as short –term capital gain or loss [2(42B)].

Short term capital gains : Any gain on transfer of short term capital asset is called short term capital gain.

It is calculated as follows :

Full value of considerations		xxx
Less: Expenses on transfer		xxx

		xxx
Net Consideration		
Less: i. Cost of acquisition	xxx	
ii. Cost of Improvement	xxx	
	-----	xxx

Short term Capital Gain		xxx

(ii) Long-term Capital Assets : Assets which do not fall within the definition given in section 2(42), i.e., the assets which are held by the assessee for a period exceeding 36 months immediately preceding the date of transfer, are called ‘long-term capital assets’.

Any gain or loss accruing on such asset shall be known as long-term capital gain or loss.[2(42B)]

The period to determine the nature of such assets which are required under transfers not regarded as transfers, shall be taken to the total period for which asset was held by previous owner and the present owner, e.g., Mr. A acquired an asset on 15th January 1989 and gifted to his son, D on 31st Dec., 1992, D sold it on 20th Feb., 2001. The transfer from A to D is not to be regarded as transfer u/s 47 and it is a long-term capital asset as it was held by Mr. A and Mr. D together, for more than 36 months.

Long –term Capital Gain: Any gain on transfer of long term capital asset is called Long –term Capital Gain (LTCG). It is calculated as follows,

Full value of consideration	xxx
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Income Tax	7.5	Income from Capital Gains
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Less: Expenses of transfer		XXX	

Net Consideration			XXX
Less: (i) Indexed cost of acquisition	XXX		
(ii) Indexed cost of improvement	XXX	XXX	

Long term Capital Gain			XXX

7.5 TRANSFER OF A CAPITAL ASSET :

Under section 2(47) of Income Tax Act, 1961, the term ‘transfer’ has been defined as: transfer in relation to a capital asset includes :

- i. The sale exchange or relinquishment of the asset; or
- ii. The extinguishment of any rights therein; or
- iii. The compulsory acquisition thereof under any law; or
- iv. In a case where the asset is converted by the owner thereof into, or is treated by him as stock-in trade of a business carried on by him such conversion or treatment; or
- v. Any transaction involving the allowing of the possession of any immovable property to be taken or retained in part performance of a contract of the nature referred to in section 53A of the Transfer of Property Act, 1882; or
- vi. Any transaction (whether by way of becoming a member of , a acquiring shares in, a co-operative society, company or other association of persons or by way of any agreement or any arrangement or in any other manner whatsoever) which has the effect of transferring or enabling the enjoyment of, any immovable property.

In this definition the word ‘transfer’ represents the sale, exchange or relinquishment of the assets. The ownership of the asset has to change to make a complete transfer. Eric L.Kohler has defined transfer as “The passage of property usually with title, or of services from one person to another.” The asset may be transferred under free-will or under compulsion. The scheme of capital gain taxation includes both the types of transfer, voluntary or involuntary. As such any sale of asset of debtor under the court order will be ‘transfer’ under the provision of this Act.

It is immaterial whether the assets are transferred by the owner himself or on his behalf by some other person. Assets of the firm under dissolution are sold by a commissioner

or receiver under the order of court and if there is capital gain, the firm under dissolution will pay tax on such capital gain.

The compulsory acquisition of an asset by Government also constitutes 'transfer' and any gain arising from such transaction will also be considered as 'Capital Gains'. The meaning of word 'transfer' is not restricted only to transfers by act of parties: compulsory acquisition of the property also amounts to a transfer. [Vadilal Soda Ice factory Vs. CIT(1917) 80 I.T.R. 711]. "A running concern's sale by a firm to a company (newly formed) will also be considered as transfer."

7.6 SCOPE AND YEAR OF CHARGEABILITY [SECTION 45] :

A transfer does not take place merely because an agreement has been entered into or consideration is paid there under in whole or in part. The words "effected in the previous year" in section 45 denote that the title in the property has passed from the transferor to the transferee. No transfer can be said to be effected till all the formalities for transferring the title to the transferee are not completed.

The following rules can be framed in this connection :

- (i) In respect of transaction concerning immovable property worth ₹ 100 or above, no capital gain can be charged to tax so long as there is no registration deed or transfer- though possession might have been given to the buyer.
- (ii) The charge of capital gain arises only when there has been a duly executed and registered deed of transfer.
- (iii) The year of assessment would be the year corresponding to the previous year in which such transfer is completed.
- (iv) Whether the consideration is paid at the time of transfer or made payable in future, is immaterial, the charge will be levied in the year in which transfer of title takes place.

7.6.1 General Provision [Section 45(1)] :

The capital gain is deemed to be the income of the previous year in which the transfer takes place. As such any capital gain should be assessed in the assessment year corresponding to the previous year in which transfer took place.

7.6.2 Insurance receipts [Section 45(1A)] :

Where any person receives any money or other assets under any insurance from an insurer on account of damage to or destruction of any capital asset, as a result of –

- Flood, typhoon, hurricane, cyclone, earthquake or other convulsion of nature; or
- Not or civil disturbance; or
- Accidental fire or explosion; or

- Action by an enemy or action taken in combating an enemy (whether with or without declaration of war), then,

Any profits or gains arising from receipt of such money or other assets shall be chargeable to income tax under the head 'Capital Gains' and shall be deemed to be the income of such person for the previous year in which such money or other asset was received.

Full value of consideration: In order to compute capital gains, the value of any money or the fair market value of other assets on the date of such receipt shall be deemed to be the full value of the consideration received or accruing as a result of the transfer of such capital asset.

7.6.3 Unit Linked Insurance Policy Receipts 45 (1B) :

Where any person receives, at any time during any previous year, any amount, under a ULIP issued on or after 1.2.2021, to which exemption under section 10(10D) does not apply on account of –

- i. Premium payable exceeding ₹ 2,50,000 for any of the previous years during the term of such policy: or
- ii. The aggregate amount of premium exceeding ₹ 2,50,000 in any of the previous years during the term of any such ULIP(s), in case where premium is payable by a person for more than one ULIP issued on or after 1.2.2021.

Then , any profits or gains arising from receipt of such amount by such person shall be chargeable to income-tax under the head "Capital gains" and shall be deemed to be the income of the such person for the previous year in which such amount was received. The income taxable shall be calculated in such manner as may be prescribed.

7.6.4 Deemed Transfer [Section 45(2)] :

In case a capital asset is converted into stock-in-trade, or is treated as stock-in-trade by the assessee it will be deemed to have been transferred. The difference between market value and the cost price shall be taxable as capital gain under this head.

7.6.5 Transfer of Capital Assets by a person to firm, AOP or body of individuals [Section 45(3)] :

When a person transfers his capital asset to a firm, AOP or body of individuals in which he is or becomes partner or member by contributing capital or otherwise, profit or gain from such transfer shall be chargeable to tax as his income of the previous year in which such transfer takes place and for computation of capital gain, the amount recorded in the books of firm, AOP or body of individuals as the value of capital asset shall be deemed as full consideration for transferor. This provision has come into effect from 1-4-88 i.e. assessment year 1988-89.

The amount recorded in the books of firm, BOI or AOP, shall become sale price. The cost at which it was acquired by the person shall be treated as cost of acquisition.

7.6.6 Transfer of Capital Assets on dissolution of firm, AOP or body of individuals [Section 45(4)] :

When an asset is transferred by way of distribution on the dissolution of firm, AOP or body of individuals, the profit or gain arising from such transfer, shall be chargeable to tax as the income of firm, AOP or body of individuals, of the previous year in which such transfer takes place.

For computing capital gains the Fair Market Value on the date of transfer shall be deemed to be the full value of the consideration received or accruing as a result of the transfer. This provision has come into effect from 1-4-88 i.e. assessment year 1988-89.

The amount recorded in the books of firm, BOI or AOP shall be the cost of the asset and the fair market value on the date of transfer to the person shall be treated as sale price.

7.6.7 Enhancement of compensation on compulsory acquisition of assets [Section 45(5)]

In the case of compulsory acquisition of assets if the consideration is determined or is approved by Central Government, or the Reserve Bank of India and later on such consideration is enhanced by the Court or Tribunal, the capital gain shall be treated in the following manner :

- (a) The capital gain arising due to such acquisition shall be taxable in the previous year in which transfer takes place:
- (b) The enhanced compensation or consideration shall be chargeable to tax under the head "Capital Gain" of the previous year in which such year in which such amount is received by the assessee(or by any other person, if original transferor has died).
- (c) With effect from 1-4-2004 in case an asset is taken over under compulsory acquisition and assessment has been made on the basis of original compensation or enhanced compensation and later on such compensation is reduced by any authority, the assessment shall be rectified by taking the reduced compensation.[Section 45(5)(c)]

7.6.8 Sale of units purchased for deduction u/s 80CCB [Section 45(6)] :

The difference between the repurchase price of the units purchased for deduction u/s 80CCB and the capital value of such units shall be deemed to be the capital gain arising to the assessee in the previous year in which such repurchase takes place.

Capital value of such units means any amount invested by the assessee in the units eligible for deduction u/s 80CCB.

7.7 CAPITAL GAINS ON DISTRIBUTION OF ASSETS BY COMPANIES IN LIQUIDATION [SECTION 46] :

1. **In the hands of Liquidated Company :** Where the assets of a company are distributed to its shareholders on its liquidation, such distribution shall not be regarded as transfer by the company for the purposes of section 45 [section 46(1)].

The above section is restricted in its application to the circumstances mentioned therein i.e., the assets of the company must be distributed to shareholders on the liquidation of the company. However, the liquidator sells the assets of the company resulting in a capital gain and distributes the funds so collected the company will be liable to pay tax on such gains.

2. **In the hands of Shareholders :** Shareholders receive money or other assets from the company on its liquidation. They will be chargeable to income tax under the head “Capital gains” in respect of the market value of the assets received on the date of the distribution, or the moneys so received by them. The portion of the distribution which is attributable to the accumulated profits of the company is to be treated as dividend income of the shareholder under section 2(22)(c), which would be taxable in the hands of shareholders under the head “income from other sources”. The same will be deducted from the amount received/fair market value for the purpose of determining the full value of consideration for computation of capital gains.
3. **Capital Gains Tax on subsequent sale by the shareholders :** If the shareholder, after receipt of any such asset on liquidation of the company, transfers it, then fair market value on the date of distribution would be treated as cost of acquisition of such asset.

7.8 DEEMED CAPITAL GAIN :

In case an asset is transferred from a parent company to a subsidiary company or from subsidiary company to a parent company [Section 47 (iv) or (v)] and

- (a) Such capital asset is converted by the transferee company into or is treated by it as stock-in-trade before the expiry of a period of 8 years from the date of transfer, or
- (b) The parent company or its nominees cease to hold the 100% share capital of subsidiary company before the expiry of a period of 8 years from the date of transfer, the capital gain which was exempted under section 47 will become taxable as deemed capital gain of the year in which such transfer took place.
- (c) In case there is a breach of any of the conditions prescribed for exemption of capital gain on succession of a firm or a sole proprietary concern under section 47(xiii) and (xiv), the amount of gain arising from such a transfer shall be deemed to be the gain taxable in the hands of successor company in the previous year in which such breach of condition takes place.[Section 47A(3)]
- (d) With effect from assessment year 1998-99 the transferor who has transferred its membership of a recognised stock exchange and has received shares as consideration, such shares cannot be transferred for a period of 3 years from the date of transfer of membership, the amount of exemption claimed under section 47 shall be deemed as income chargeable to tax under the head capital gains. [Section 47A (2)]

Transfer in case of reverse mortgage [Section 47 (xa)] :

The Finance Bill 2008 has proposed to insert a new clause 47 (xa) in Income Tax Act to provide that any transfer of capital asset in a transaction of reverse mortgage shall not be regarded as transfer and hence shall not attract capital gains tax.

It is further provided that loans received in either in lump sum or in installment is a capital receipt and shall be exempted u/s 10.

A borrower, under the reverse mortgage scheme will be liable to income tax (i.e, tax on capital gains) only at the point of alienation of the mortgage property by the mortgagee for the purposes receiving of loan.

ILLUSTRATION – 1:

Mr. Abhishek a senior citizen, mortgage his residential house with a bank, under a notified reverse mortgage scheme. He was getting loan from bank in monthly installments. Mr. Abhishek did not repay the loan on maturity and hence gave possession of the house to the bank, to discharge his loan. How will the treatment of long term capital gain be on such reverse mortgage transaction?

SOLUTION :

Section 47 (xvi) provides that any transfer of a capital asset in a transaction of reverse mortgage under a scheme made and notified by the Central Government shall not be considered as a transfer for the purpose of capital gain.

Accordingly, the mortgaging of residential house with bank by Mr. Abhishek will not be regarded as a transfer. Therefore, no capital gain will be charged on such transaction.

Further, section 10 (43) provides that the amount received by the senior citizen as a loan, either lump sum or in installment, in a transaction of reverse mortgage would be exempt from income-tax. Therefore, the monthly installment amounts received by Mr. Abhishek would not be taxable.

However, capital gains tax liability would be attracted at the stage of alienation of the mortgaged property by the bank for the purpose of recovering the loan.

7.9 METHODS OF COMPUTING CAPITAL GAIN [SECTION 48] :**1. For all assessee and all assets except share and debentures owned by a non-resident**

- a. short-term capital gain shall be computed by deduction out of full value consideration the following amounts :
 - i. Expenditure incurred wholly and exclusively in connection with such transfer;
 - ii. the cost of acquisition of the assets; and
 - iii. The cost of any improvement thereto.

- b. Long –term capital gain shall be computed by deducting out of full value of consideration the following amount.
- i. Expenditure incurred wholly and exclusively in connection with such transfer;
 - ii. The indexed cost of acquisition; and
 - iii. The indexed cost of any improvement thereto.
- c. Where capital assets being shares, debentures or warrants as referred in section 47(iii) are transferred under a gift or irrevocable trust the market value on the date of transfer shall be deemed to be the full value of consideration received or accruing as a result of transfer.

Expenses disallowed u/s section 48 :

Any amount paid on account of Security Transaction Tax shall be allowed to be deducted u/s 48.

For the above purpose :

- A. **“Indexed cost of acquisition”** means an amount which bears to the cost of acquisition the same proportion as Cost Inflation Index for the first year in which assets was held by the assessee or for the year beginning on the 1st day of April 1981, whichever is later.
- B. **“Indexed cost of any improvement”** means the amount which bears the cost of improvement the same proposition as cost Inflation Index for the year in which the assets is sold bears to the cost Inflation Index for the year in which improvement to the assets took place.
- C. **“Cost Inflation Index”** in relation to a previous year, means such index as the central government may, having regard to seventy five per cent of average rice in the consumer Price Index for urban non-manual employees for the immediately preceding previous year to such previous year, by notification in the official Gazette, specify, in this behalf.

The cost inflation indices for the financial years so far been notified as under :

Financial –year	Cost Inflation Index
2001-02	100
2002-03	105
2003-04	109
2004-05	113
2005-06	117
2006-07	122
2007-08	129
2008-09	137
2009-10	148
2010-11	167

2011-12	184
2012-13	200
2013-14	220
2014-15	240
2015-16	254
2016-17	264
2017-18	272
2018-19	280
2019-20	289
2020-21	301
2021-22	317
2022-23	331
2023-24	348

C.I.I = COST INFLATION INDEX

ILLUSTRATION – 2 : Cost of acquisition in 2001-02 ₹ 4,00,000. Find out the indexed cost if sold in 2021-22 [C.I.I for 2001-02 is 100 and for 2021-22 is 317].

SOLUTION :

Computation of indexed cost

Cost in 2001-02 = ₹4,00,000

Indexed cost = ₹4,00,000 x 317/ 100 = ₹12,68,000

Computation of Capital Gain in Case of Non-Residents [Section 48 proviso 1]

This proviso is available to non-residents only.

The non-residents must have acquired shares or debentures of Indian companies using foreign currency.

Such non-residents, wanting to transfer such share will follow the following considerations and conditions.

The asset may be short term or long term.

The capital gain from transfer of such asset shall be computed in the following manner :

- (i) Capital gain is computed in the same currency in which shares were acquired
- (ii) Sale consideration in Indian currency is converted into foreign currency at average exchange rate on the date of transfer.
- (iii) Cost of acquisition in Indian currency is converted into foreign currency at average exchange rate on the date of acquisition.

- (iv) Expenditure incurred in Indian currency on sale is converted into foreign currency at average exchange rate on the date of transfer.
- (v) Out of sale consideration in foreign currency as per (ii) above cost of acquisition as per (iii) above and expenses on sale as per (iv) above are deducted.
- (vi) Cost of acquisition of such shares and debentures is not to be indexed u/s 48.
- (vii) Balance amount is capital gain which is reconverted into Indian currency at buying rate on the date of transfer.
- (viii) **“Average exchange rate”**-- It is the average of telegraphic transfer buying rate and telegraphic transfer selling rate of exchange adopted by the State Bank of India for purchasing or selling such currency through telegraphic transfer.

ILLUSTRATION – 3 : Mr.Rohan a non-resident sent ₹1,45, 000 to India on 20th May 2013. On July 7, 2013 a part of this money was utilised to purchase ₹1,20,000 shares of ABC Ltd. An Indian company @ ₹10 per share on .1-10-2023 these shares were sold @ ₹ 30 per share. Compute the capital gain if telegraphic transfer rates are as follows :

	20-5-2013 (for US\$)	7-7-2013 (for US\$)	1-10-2023 (for US\$)
	₹	₹	₹
Buying rate	59	60	68
Selling rate	60	61	69

SOLUTION :

Computation of capital gain of non-resident

Calculate Average Exchange Rate on	7-7-2013	1-10-2023
	₹	₹
Buying rate	60	68
Selling rate	61	69
Total	121	137
Average Exchange Rate	60.50	68.50
Conversion of sale price into foreign currency At Average Exchange Rate on date of transfer 1, 20, 000 x 30/68.50	52, 554.744	
Conversion of cost of acquisition in to foreign currency At Average Exchange Rate on the date of transfer 1, 20, 000 x 10/60.50	19, 834.711	

Long term capital gain	72, 389.455
Convert this capital gain into Indian currency at Buying rate on the date transfer 72, 389. 455 x 68.00	49, 22, 482.94

This gain shall be fully exempted u/s 10(38) if such transaction was entered through stock exchange and was Subject Transaction Tax [STT].

Q.NO.1

Mr. P. Kumar a non-resident sent \$ 1,80,000 to India on 1-7-2012. On 1-11-2012 part of this money was utilised to purchase 1500 shares of X Ltd. an Indian company @ ₹ 300 per share. On 15-3-2023 these shares were sold @ ₹ 640 per share. Compute the capital gain if telegraphic transfer rates are as follows:

	1-7-2012 (for US\$) ₹	1-11-2012 (for US\$) ₹	15-3-2023 (for US\$) ₹
Buying Rate	58	59	68
Selling Rate	59	60	69

Determination of Cost of Acquisition :

The cost of acquisition means the price which an assessee has paid to purchase, construct or acquire an asset. No problem arises in finding out the cost of acquisition in case of assessee purchasing, constructing or acquiring the asset himself. But in other cases there are different rules to determine the cost of acquisition. They are :

1. **In case of assets acquired without paying any price [49 (1)].** Where the asset has become the property of the assessee in any of the ways enumerated below, the cost of acquisition shall be deemed to be the cost at which previous owner had acquired the same plus cost of any improvement by the said previous owner and after deducting depreciation allowed by him. These cases are:
 - (i) any division of assets by H.U.F. among its members on its partial or total partition;
 - (ii) assets received under a gift or will;
 - (iii) (a) assets received under succession, inheritance or devolution; or
 - (b) any distribution of assets on the dissolution of firm, body of individuals or other association of persons where such dissolution takes place before 1-4-1987; or
 - (c) Any distribution of assets on liquidation of a company; or
 - (d) A transfer to a revocable or irrevocable trust; or

- (e) Any such transfer from a parent company to its wholly owned subsidiary Indian Company or vice versa.
- (iv) any transfer of asset by an individual into the common pool of H.U.F.- the cost to H.U.F will be the cost borne by individual.
2. **Shares in amalgamated company [49 (2)].** In case of amalgamation of a company into an Indian company the cost of acquisition of shares of amalgamated company shall be taken to be the cost of acquisition to him of the shares of the amalgamating company.
 3. The cost of shares received on conversion of debentures, deposit certificates or debenture stock shall be the cost at which original asset was acquired [Section 49(2A)].
 4. **Cost of Acquisition of the Shares, debentures or Warrants [Section 49(2AA)].** With effect from assessment year 2001-02 where the capital gain arises from the transfer of shares, debentures or warrants the value of which has been taken into account as perk under the head salary, the cost of such assets shall be taken as the same value which was taken as value of the perk.
 5. **Cost on sale of security received as perk [Section 49(2B)].** In case any specified security received by an employee and which has been treated as perquisite u/s 17(2)(iiia), is transferred the cost of acquisition of such security shall be its fair market value on the date of exercise of option.
 6. **Cost of Shares of resulting company [Section 49(2C)].** The cost of acquisition of shares of resulting company as a result of merger shall be:

Cost of acquisition of shares held	Net Book Value assets transferred
by the assessee in the demerged	X-----
Company	Net worth of demerged company before demerger
 7. **Cost in case of deemed capital gain u/s 47 A [Section 49(3)].** Where the capital gain arising from the transfer of a capital asset is deemed to be income chargeable under the head capital gains as a result of operation of provisions of section 47A, the cost of acquisition of such asset to the transferee company shall be the cost for which such asset was acquired by it.

Computation of capital gains in case depreciable assets [Section 50 & 50A] :

Section 50 : Provides for the computation of capital gains in case of depreciable assets. It may be noted that where the capital asset is a depreciable asset forming part of a block of assets, section 50 will have overriding effect in spite of anything contained in section 2(42A) which defines a short-term capital asset.

Section 50A : With respect to the power sector, in case of depreciable assets referred to in section 32(1)(i), the provisions of sections 48 and 49 shall apply subject to the

modification that the WDV of the asset [as defined in section 43(6)], as adjusted, shall be taken to be the cost of acquisition.

Profit / Loss on Slump Sale [Section 50(b)] :

1. Any profit and gains arising from 'slump sale' effected in the previous year shall be chargeable to tax as capital gains and shall be deemed as income of the previous year in which transfer takes place. In case asset was held for a period not exceeding 36 months it shall be a short term capital asset and if held for a period exceeding 36 months it shall be long term capital asset.
2. "Net worth" shall be the aggregate value of total assets of the undertaking or division as reduced by the value of liabilities of such undertaking or division as appearing in its books of accounts but any change in the value of assets on accounts of revaluation of assets shall be ignored for the purpose of computing the net worth.

For computing the net worth, the aggregate value of total assets shall be :

- (a) In the case of depreciable assets, the written down value of the block of assets determined in accordance with the provisions contained in sub-item (C) of item (1) sub-clause (c) of clause (6) of section 43; and
 - (b) In the case of other assets, the book value of such assets.
3. Every assessee having 'slump sale' shall furnish a report along with its return of income, from a Chartered accountant certifying that the net worth has been currently calculated.
 4. The cost of such asset shall be reduced by such advanced money received and forfeited by the assessee. In case FMV on 1-4-1981 is adopted and advanced money is received either before or after this date and is forfeited, it shall be reduced out of the F.M.V.

Cost of acquisition of assessee forfeiting advance money = Cost of acquisition or W.D.V. or F.M.V. as on 1-4-1981 – Advance money received and forfeited

Important Note : Advance money is to be reduced from cost of acquisition/WDV/FMV on 1-4-81 only while computing capital gain from such asset for the assessee who had received and forfeited the advance money in the past. Thus, where such an assessee transfers this capital asset to another person as per section 49 (1) i.e., by way of gift, will etc., advance money forfeited by assessee transferring capital asset shall be reduced from cost /WDV/FMV as on 1-4-81 while computing capital gain for the assessee who acquires such asset as per section 49(1)

To put it simply, advanced money forfeited by previous owner shall not be reduced from cost/WDV/FMV, while computing capital gain for the person acquiring capital asset without any price u/s 49(1)

Advanced money forfeited by current owner transferring a capital asset →

Advance money received is to be reduced to find out cost of acquisition

Advanced money forfeited by any other previous owner → Advance money received and forfeited by any other previous owner will not be reduced while calculating cost of acquisition.

5. In case advance money received and forfeited is more than cost of acquisition of such asset, nothing shall be taxable at the time of receipt. As and when such asset is sold, the excess of amount received and forfeited over cost of acquisition shall be assessed to tax as capital gain.
6. If the amount of advance money is forfeited due to fault to buyer, it shall not be treated as capital loss in the hands of buyer but if advance money is received along with additional compensation due to the fault, of seller, additional compensation received from seller shall be treated as capital gain in the hands of buyer.

ILLUSTRATION – 4 : Mr.Rohan sold an house on 1-9-2021 for ₹ 7,00,000. This house was inherited by him during 2001-02 from his father who had constructed it in 1991-92 for ₹ 50,000. Mr.Rohan spent ₹ 50,000 on renovation of the house in 2006-07. Fair market value of the house as on 1-4-2001 was ₹ 1,50,000.

This was under negotiations for sale in May, 2010 and he received ₹ 80,000 as advance money. The contract could not materialize and the advance money was forfeited. Compute the amount of capital gain assuming that he does not qualify for any exemption.

[C.I.I. for 2001-02: 100, 06-07:122, 10-11:167 & 2021-22: 317]

SOLUTION :

Computation of Capital Gain (Assessment Year 2022-23)

Particulars	Amount (₹)	Amount (₹)
Sale Price on 1-9-2021		7,00,000
Less: Cost of acquisition	1, 50, 000	
Less: Advance money forfeited	80, 000	
Net cost	70, 000	
Indexed cost [70,000 X 317/100]	2, 21,900	
Indexed cost of improvement [50,000 X 317/122]	1,29,918	3, 51, 818
Long Term Capital Gain		3, 48, 182

Q.NO. – 2 :

Mr. V. Krishna received a gift of a house in Nov.2017 from Mr. K. Narayana who had purchased it in Nov.1997 for ₹ 6,30,000. Mr. K. Narayana renovated the house in March 2000 at a cost of ₹ 2,70,000. Its FMV on 1-4-2001 was ₹ 12, 60, 000. In 1999-2000 Mr.K. Narayana had agreed to sell the house and had received ₹ 1,00,000 as advance money. The sale could not materialize and advance money was forfeited. The house was further renovated in 2007-2008 [C.I.I. =] at a cost of ₹ 1,00,000. Mr. Krishna sold the house in

December 2022 for ₹40,60,000 and paid ₹ 60,000 as brokerage. Compute his taxable capital gain if C.I.I. for 2001-2002 was 100, for 2017-2018 was 272 and for 2021-22 it is 317.

EXPENDITURE INCURRED IN CONNECTION WITH TRANSFER :

The cost of stamp and registration fees, brokerage, commission and travelling expenses etc., incurred in connection with transfer to the transferee are allowed to be deducted from the full consideration.

7.10 EXEMPTIONS IN RESPECT OF CERTAIN CAPITAL GAINS :

Capital gain arising on transfer of certain capital assets has been exempted from tax. In other words in certain cases capital gain does not become part of total income due to some specific exemptions granted under Income Tax Act 1961. These specific exemptions can broadly be classified into following two categories:

- (A) Capital gains exempted u/s 10
- (B) Capital gains exempted u/s 54

A. CAPITAL GAINS EXEMPTED U/S 10 :

1. Income from sale of shares in certain cases [Section 10(36)] :

Any income arising from the transfer of a long-term capital asset, being an eligible equity shares in a company purchased on or after the 1st day of March, 2003 and before the 1st day of March 2004 and held for a period of twelve months or more shall be fully exempted.

2. Capital gain on compulsory acquisition of urban Agricultural land [Section 10(37)] :

In the case of an assessee, being an individual or a Hindu undivided family, any income chargeable under the head “Capital Gains” arising from the transfer of agricultural land, shall be exempted; where

- (i) Such land is situate in any urban area as specified u/s 2(14)(iii) (a) or (b) i.e. land which is situated within the Municipal limits or within 8 kms. Of city limits, if so notified;
- (ii) Such land ,during the period of two years immediately preceding the date of transfer, was being used for agricultural purposes by such Hindu undivided family or individual, or a parent of his;
- (iii) Such transfer is by way of compulsory acquisition under any law, or a transfer the consideration for which is determined or approved by the Central Government or the Reserve Bank of India;
- (iv) Such income has arisen from the compensation or consideration for such transfer received by such assessee on or after the 1.4.2004.

For the purposes of this clause, the expression, compensation or consideration includes the compensation or consideration enhanced or further enhanced by any court, tribunal or other authority.

ILLUSTRATION – 5 :

Mr. Rohan has an agricultural land costing ₹ 6, 00, 000 in Lucknow on 1.4.2003 and has been using it for agricultural purposes till 1.8.2012 when the Government took over compulsory acquisition of this land. A compensation of ₹ 12, 00, 000 was settled. The compensation was received by Mr. Rohan on 1.7.2021. Compute the amount of capital gains taxable in the hands of Mr. Rohan.

(C.I.I: 2003-04:109, 2012-13: 200, 2021-22: 317)

SOLUTION :

In the given problem, compulsory acquisition of an urban agricultural land has taken place and the compensation is received after 1.4.2004. This land had also been used for at least 2 years by the assessee himself for agricultural purposes. Thus, as per section 10(37), entire capital gains arising on such compulsory acquisition will be exempt and nothing is taxable in the hands of Mr. Rohan in the year of receipt of compensation i.e., A.Y 2022-23.

Computation of capital gains

Particulars	Amount (₹)
Sales consideration	12, 00, 000
Less: Cost of acquisition (6, 00, 000 x 200/109)	11, 00, 917
Long –term Capital Gains	99, 083

B. EXEMPTED CAPITAL GAIN u/s 54 :

Section 54 provides for exemption in respect of long term capital arising on transfer certain capital assets. However, in order to claim these exemptions the assessee is required to invest either net consideration or capital gain in certain specified assets. Besides this, an assessee is required to fulfill certain conditions specified in relevant sections granting the exemption. These exemptions are covered u/s 54, 54B, 54D, 54F, 54G, and 54GA and are as follows :

1. Capital gain on transfer of long term residential house property [Section 54] :

When on the transfer of a house property or land appurtenant thereto being taxable under the head 'income from house property' owned by an individual and H.U.F. there occurs some capital gain and such capital gain is reinvested in:

- (a) Purchase of another residential house within one year or two years after the sale of the house or
- (b) Construction of new residential house within three years after the sale of the house.

The amount of capital gain so invested shall be exempted from tax.

A residential house property purchased or constructed by re-invested capital gain cannot be transferred within 3 years of its purchase or construction.

If the house so acquired by reinvesting capital gain is sold within period of three years from the date of purchase or construction, the previously exempted capital gain will be taxable along with the capital gain on the sale of such house, if any, in the current previous year. In the event of loss on sale of new house, it shall be adjusted out of old exempted capital gain [Section 54].

In case the amount of capital gain is not re-invested for the purchase or construction of the new house upto the last date of filing of return of income u/s 139 then it should be deposited in the capital gain deposit account scheme with a specified bank authorised by the central government in accordance with the scheme. Any amount already utilized by the assessee for the purchase or construction of the new house together with the amount so deposited shall be deemed to be the cost of new house.

ILLUSTRATION – 6 :

Mr. Ravi purchased a residential house on July 20, 2019 for ₹10, 00,000 and made some additions to the house incurring ₹ 2, 00, 000 in August 2019. He sold the house property in April, 2021 for ₹ 20, 00, 000. Out of the sale proceeds, he spent ₹ 5, 00, 000 to purchase another house property in September, 2021. What is the amount of capital gains taxable in the hands of Mr. Ravi for the .Y.2022-23?

SOLUTION :

The house is sold before 24 months from the date of purchase. Hence, the house is a short-term capital asset and no benefit of indexation would be available.

Particulars	Amount (₹)
Sale consideration	20, 00, 000
Less: Cost of acquisition	10, 00, 000
Cost of improvement	2, 00, 000
Short-term Capital Gain	8, 00, 000

Note : The exemption of capital gains under section 54 is available only in case of long-term capital asset. As the house is short-term capital asset. Mr. Ravi cannot claim exemption u/s 54. Thus, the amount of taxable short-term capital gains is ₹ 8, 00 000.

3. Capital gain on transfer of self – cultivated agricultural land in urban areas [Section 54 B] :

When on the transfer of agricultural land, which was being used for agriculture purpose by the assessee or his parents for a period of at least two years immediately preceding the year of a transfer and there occurs some capital gain and such capital gain is

reinvested in the purchase of agricultural land within a period of 2 years from the date of such transfer, the amount of capital gain so invested shall be exempted from tax.

If the land, so purchased by reinvesting the capital gain, is transferred within a period of 3 years from the date of its purchase, the previously exempted capital gain will be taxable along with the new capital gain on the sale of such land, if any in the current previous year.

Agriculture land situated in rural areas is not treated as capital asset and so capital gain arising from sale of agricultural land in rural areas is not changeable to tax.

In case the amount of capital gain is not re-invested for the purchase of agricultural land upto the last date of filing of return of income u/s 139 then the amount of capital gain should be deposited in the capital gain deposit account scheme with a specified bank upto the last date of filing of return. The proof of deposit is required to be attached with the return of income of that year.

The amount deposited under this scheme must be utilized to purchase agricultural land within 2 years from the date of transfer of agricultural land. In case amount deposited is not utilized purchase agricultural land within the stipulated period, than the amount which remains unutilized shall be treated as capital gain of the previous year in which the period of 2 years would expire.

3. Capital gain on compulsory acquisition of land and building [Section 54 D] :

Where the capital gain arises from the transfer by way of compulsory acquisition under any law, if a capital asset being land or building or any right in land or building forming part of an industrial undertaking, which was being used by assessee for 2 years preceding the previous year in which the asset was acquired for his own business and the assessee reinvests capital gains from a such transfer in purchase of another land or building or right in land or building or constructs another building within 3 years after the transfer, the capital gain so invested is exempted from tax. If the amount invested is less than the capital gain earned, the balance shall be taxable.

The new asset so purchased cannot be sold or transferred within a period of 3 years from the date of transfer. If sold or transferred earlier, old exempted gain along with new capital gain will be taxable in the previous year in which new asset is transferred.

ILLUSTRATION – 7 :

ABC Ltd., purchased a land for industrial undertaking in May 2004, at a cost of ₹ 3, 50, 000. The above property was compulsorily acquired by the State Government at a compensation of ₹ 12. 00, 000 in the month of January, 2022. The compensation was received in February 2022. The company purchased another land for its industrial undertaking at a cost of ₹ 2, 00, 000 in the month of March, 2022. What is the amount of the capital gains chargeable to tax in the hands of the company for the A.Y. 2023? (C.I.I. 204-05: 113, 2021-22: 317)

SOLUTION :

Computation of capital gains in the hands of ABC Ltd. for the A.Y.2022-23

Particulars	Amount (₹)
Sale proceeds (Compensation received)	12, 00, 000
Less: Indexed cost of acquisition (3, 50, 000X 317/113)	9, 81, 858
Less: Exemption u/s 54 D (Cost of acquisition of land for its Undertaking)	2, 18, 142 2, 00, 000
Taxable long –term capital gain	18, 142

4. Capital gain on transfer of any long term capital asset [Section 54 EC] :

In case the capital gain arises from the transfer of a long term capital asset (to be called as the original asset) and the assessee has at any time within a period of six months after the date of such transfer, invested the whole or any part of capital gains in the long term specified asset, such capital gain shall be exempted in accordance with the following provisions of the section :

- (a) If, whole of such capital gain is reinvested in the long term specified asset the whole of such capital gain shall be exempted.
- (b) If, the amount of the long term gain is reinvested in the long term in specified asset is less than the capital gain arising from the transfer of the original asset, amount so invested in specified asset shall be exempted. [Section 54 EC(1)]

Where the long term specified asset is transferred or converted otherwise than by transfer into money at any time within a period of 3 years from the date of its acquisition, the amount of capital gains arising from the transfer of the original asset not charged under section 45 on the basis of the cost of such long term specified asset as provided in clause (a), or as the case may be, clause (b) of sub-section (1) shall be deemed to be the income chargeable under the head ‘capital gains’ relating to long term capital asset of the previous year in which the long term specified asset is transferred or converted into money.

In a case where the original asset is transferred and the assessee invests the whole or any part of capital gain received accrued as a result of transfer of the original asset in any long term specified asset and such assessee takes any loan or advance on the security of specified asset under section 54 E (2).

5. Exemption of capital gain on transfer of long term capital assets in case of investment in residential house [Section 54 F] :

In case an individual and HUF transfer any long-term capital asset (other than the residential house the income of which is taxable under the head ‘Income from house property’) and constructs a residential house within 3 years after the sale or purchases another residential house within one year before or two years after the sale, so much of capital gain shall be exempted as is in proportion of amount invested to net consideration.

Exemption u/s 54-F shall be allowed if following conditions are fulfilled.

- (i) The assessee is only an individual or a H.U.F.
- (ii) The assessee does not own more than one residential house on the date of transfer of the above mentioned assets.
- (iii) The assessee transfers above mentioned asset or assets (other than a residential building) and there is a long term capital gain.
- (iv) The assessee invests the net sale consideration of above mentioned assets to construct a residential house within 3 year of the sale of the asset or purchases an already built a house within one year before or two years after the sale of the above mentioned asset.
- (v) The assessee is required not to purchase another residential house within a period of one year after or constructs within a period of 3 year after the date of transfer of the above mentioned asset/assets.

ILLUSTRATION – 8 :

From the following particulars, compute the taxable capital gains of Mr. Vinay for A.Y. 2023.

Particulars	Amount (₹)
Cost of Jewellery (Purchased in F.Y. 2005-06)	4, 52, 000
Sale price of Jewelery sold in January 2022	12, 50, 000
Expenses on transfer	7, 000
Residential house purchased in March 2022	5, 00, 000

(C.I.I 2005-06:117, 2021-22: 317)

SOLUTION :

Computation of taxable capital gains Mr. Vinay, for A.Y.2022-23

Particulars	Amount (₹)
Gross Consideration	12, 50, 000
Less: Expenses on transfer	7, 000
Net consideration	12, 43, 000
Less: Indexed cost of acquisition (4, 52, 000 x 317/117)	12, 24, 650
	18, 350
Less: Exemption u/s 54 F (18, 350 x 5, 00, 000 / 12, 43, 000)	7, 381
Taxable long-term capital gain	10, 969

6. Capital gain on shifting of industrial undertaking from urban areas to non-urban areas [Section 54 G] :

In case following conditions are fulfilled, the capital gain shall be exempted as per rates given below :

- (i) Capital asset (P & M, Land, buildings or any right therein) is transferred due to shifting of industrial undertaking from urban areas to rural areas: and
- (ii) Capital gains reinvested within a period of 1 year before or 3 years after the date in:
 - (a) Purchase of new machinery or plant for the purpose of the business of the industrial undertaking in the area to which the said undertaking is shifted;
 - (b) Acquiring building or land or construction of building for the purpose of business in the said area;
 - (c) Shifting the original asset and transferring the establishment of such undertaking to such area; and
 - (d) Incurred expenses on such other purposes as may be specified in a scheme framed by the Central Government for the purposes of this section.

Amount of exemption. In case above- mentioned conditions are fulfilled the amount of exemption under this section will be :

- (i) If the amount of the capital gain is greater than the cost and expenses incurred in relation to all or any of the purposes mentioned in clauses (a) to (d) (such cost and expenses being hereafter in this section referred to as the new asset), the difference between the amount of the capital gain and the cost of the new asset shall be charged under section 45 as the income of the previous year; and for the purpose of computing in respect of the new asset any capital gain arising from its transfer within a period of three years of its being purchased, acquired, constructed or transferred, as the case may be, the cost shall be nil; or
- (ii) If the amount of the capital gain is equal to, or less than the cost of the new asset, the capital gain shall not be charged under section 45; and for the purpose of computing in respect of the new asset any capital gain arising from its transfer within a period of 3 years of its being purchased, acquired, constructed or transferred, as the case may be the cost shall be reduced by the amount of the capital gain.

7. Exemption of capital gain on transfer of assets in case of shifting of industrial undertaking from an urban area to any special economic zone (SEZ) [Section 54 GA] :

W.e.f. A.Y. 2006-07 this exemption has been introduced to encourage industrial Undertaking situated in an urban area to shift to a Special Economic Zone. This exemption is expected to help those industrial undertaking which may shift their premises from an urban area to a Special Economic Zone.

To avail this exemption, following points are to be noted :

- 1 There is a transfer of assets like land and building or any right in land and building, plant and machinery of an industrial undertaking situated in an urban area.

- 2 The above mentioned transfer has been made with the intention of shifting of an industrial undertaking from an urban area to a Special Economic Zone.
- 3 In connection with transfer of an industrial unit from an urban area to a Special Economic Zone, the assessee has set up an industrial unit in an Economic Zone within a period of one year before or 3 years after the date on which such transfer took place.

This means that the assessee has bought land or acquired or constructed a building, purchased plant and machinery or has shifted the original assets and has transferred the establishment from an urban area to a Special Economic Zone within the time frame of one year before and 3 years after the date on which the above mentioned transfer took place.

Amount of Exemption :

Least of following two amounts shall be the exemption :

1. Amount of Capital Gain earned on the transfer of Capital Asset.
2. Amount spent on the purchase, construction etc. of new assets in a Special Economic Zone within specified time frame.

No transfer of new assets within 3 years New assets acquired by invested the amount of Capital Gain are not supposed to be transferred within 3 years from the date of their purchase, construction etc. and if transferred exemption allowed earlier u/s 54GA shall be withdrawn and so Capital Gain arising from such transfer and Capital gain got exempted earlier, both will be taxed in the year in which transferred.

7.11 SUMMARY :

Capital gains tax can often be complicated to estimate. Apart from the taxes, there are also a small amount of cess and surcharge applicable. In terms of tax, having long-term holdings are better than short-term holdings, as you have to pay a 15% tax on short-term capital gains. Investing in listed securities and equity-oriented mutual funds for long-term holdings also works out better as the capital gains from these sources is not subject to tax.

7.12 KEY WORDS :

- AOP** : An Association of Persons
BOI : A Body of Individual
CII : Cost Inflation Index
ESOP : Employee Stock Ownership Plan
FMV : Fair Market Value
HUF : Hindu Undivided Family
LLP : Limited Liability Partnerships
LTCG : Long-term Capital Gain
RFCTLAR Act 2013 : Right to Fair Compensation and Transparency in Land Acquisition, Rehabilitation and Resettlement Act, 2013
STCG : Short-term Capital Gain

STT	:	Subject Transaction Tax
ULIP	:	Unit-Linked Insurance Plan
WDV	:	Written-Down Value

7.13 SELF ASSESSMENT QUESTIONS :

1. Define the 'capital gain'? Discuss the procedure for computation of capital gain as prescribed by the income tax act, 1961.
2. What is the meaning of the term, 'cost of acquisition' as used in the head capital gains? What rules are given for the determination of cost of acquisition?
3. How will you distinguish between capital gain and income? Why is it important to make this distinction?
4. Write short notes on :
 - i. Transfer
 - ii. Capital Gains
 - iii. Long-term and Short-term Capital Assets and Gains
 - iv. Capital Improvement
5. Giri has acquired a residential house property in Mumbai on 15th April, 2002 for ₹ 9,00,000 and decided to sell the same on 3rd May, 2005 to M/s. Rani and an advance of ₹ 25,000 was taken for her. The balance money was not paid by M/s. Rani and Giri has forfeited the entire advance sum. On 3rd June, 2021, he has sold this house to Mr.Suri for ₹40,000 on 4th April, 2021 he had purchased a residential house in Delhi for ₹8,00,000, where he was staying with his family on rent for the last 5 years and paid the full amount as per the purchase agreement. However, Giri does not possess any legal title till 31st March, 2022 as such transfer was not registered with the registration authority.

Giri has purchased another old house in Chennai on 14th October, 2021 from Mr. X, an Indian resident, by paying ₹ 5,00,000 and the purchase was registered with the appropriate authority.

Determine the taxable capital gain arising from above transactions in the hands of Giri for Assessment Year 2022-23.

[Cost Inflation Index: 2002-03: 105; 2005-06: 117;2021-22: 317]

7.14 SUGGESTED READINGS :

1. V.P.Gaur and D.R.Narang, 'Income Tax Law and Practice', Kalyan Publication House, New Delhi.
2. Mahendra B. Gabhawala, 'Direct Tax Ready Reckoner with Planning', Bharat Law House Pvt. Ltd, 2019.

3. Dr Vinod K .Singhania and Dr Kapil Snghania, 'Direct Taxes Law and Practice', Taxmann, 2023.
4. Dr Girish Ahuja and Dr Ravi Gupta, 'Direct Tax Ready Reckoner with Planning', Commercial Law Publisher (India) Pvt. Ltd, 2023.
5. Income tax act, Bharat Law House Pvt. Ltd.

Dr. Vishnu Vadde

Lesson – 8

INCOME FROM OTHER SOURCES

Objectives :

The objectives of the lesson are :

- To understand the nature of the head 'income from other sources;
- To know the deduction allowable and deduction not allowable while computing income under this head;
- To describes the profits chargeable to tax ; and
- To acquaint the method of accounting under this head.

Structure of the lesson :

- 8.1 Introduction
- 8.2 Nature of the Head [Section 56]
- 8.3 General Incomes [Section 56 (1)]
- 8.4 Specific Incomes[Section 56 (2)]
- 8.5 Deductions Allowable [Section 57]
- 8.6 Deductions Not Allowable [Section 58]
- 8.7 Profits Chargeable to Tax [Section 59]
- 8.8 Method of Accounting [Section 145]
- 8.9 Summary
- 8.10 Key Words
- 8.11 Self Assessment Questions
- 8.12 Suggested Readings

8.1 INTRODUCTION :

Rights and Powers of an Auditor –

An auditor must have certain powers to perform his duties honestly and successfully. The conferred rights and powers of the auditor cannot be restricted or curtailed by the Articles of Association of the Company or by the Board.

Any incomes, profits or gains includible in the total income of an assessee, which cannot be included under any of the proceeding heads of income, is chargeable under the head 'income from other sources'. Thus, this head is the residuary head of income and brings within its scope all the taxable income, profits or gains of an assessee which fail outside the

scope of any other head. Therefore, when any income, profit or gain does not fall precisely under any of the other specific heads but is chargeable under the provisions of the Act, it would be charged under this head.

8.2 NATURE OF THE HEAD [SECTION 56] :

The fifth and residuary head of income is “Income from Other Resources”. Every income which does not specifically fall under any of the preceding four heads shall be included in this head. Section 56 in its sweeping language embraces anything which can be described as income and it is taxable under the act unless expressly exempted. This section operates only where a particular income cannot be included in any other head.

Under section 56 (1) every kind of income which included in the total income under this Act and which is not chargeable to tax under any of the first four heads specified in section 14 is chargeable to income tax under the head ‘Income from Other Sources’.

Under section 56 (2), in particular, the following incomes shall be chargeable to income tax under the head ‘Income from Other Sources’ :

1. Dividends

- 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. These can be called as casual incomes.
- With effect from 1-4-87, i.e., assessment year 1988-89 any sum received by assessee from his employees as contribution to any provident fund or superannuation fund or any fund set up under the provisions of the Employees State Insurance Act, 1948 or any other fund for the welfare of such employees [Section 2(24) (X)] if such income is not chargeable to tax under the head “Profits and Gains of Business or Profession”.

2. Any income by way of interest on securities if the income is not chargeable to tax under the head “Profits and Gains of Business or Profession”.

- Income from machinery, plant and furniture belonging to the assessee and let on hire, if the income is not chargeable to income-tax under the head “Profits and Gains of Business or Profession”.
- Where an assessee lets on hire machinery, plant and furniture belonging to him and also building and the letting of the building is inseparable from the letting of the said machinery, plant and furniture, the income from such letting if it is not chargeable to income-tax under the head “Profits and Gains of Business or Profession”.
- Where any sum of money aggregate value of which exceeds fifty thousand rupees is received without consideration by an individual or a H.U.F. in any previous

year from any non relative person or persons the whole of the aggregate value is chargeable to tax.

- Any sum received under a key man insurance policy including bonus if such a sum is not taxable as salary or business income.

8.3 GENERAL INCOMES [SECTION 56(1)] :

Under the provisions of Section 56(1), the head will operate only when the first four heads of income are exhausted. The onus will be on the assessee to prove that particular income does not fall under any of the preceding four heads.

- i. Income derived by a coal mine owner from rent and royalties are included in this head.
- ii. Income earned by an assessee from licenses granted to brick-makers, to erect bricking upon his land and to take away the brick-earth and use it for making bricks.
- iii. Remuneration received merely for being a director and not as employees, is not salary but income from other sources.
- iv. Income received by an assessee from a person other than his employer e.g. university remuneration.
- v. Interest on loans, securities, deposits and current account also come under this head.
- vi. Income received by professional man as a university examiner.
- vii. Income received on sub-letting of the house.
- viii. Tips received by a waiter or taxi driver, not being given by his employer.
- ix. Family pension received by legal heirs of employee.
- x. Deemed incomes.
- xi. Income from other persons to be included in the income of individual.
- xii. Income from writing articles by non-journalist.
- xiii. Any withdrawal from National Saving Scheme upto an amount on which deduction u/s 80CCA has been claimed.
- xiv. Income from agricultural land situated outside India.
- xv. Remuneration for lectures delivered outside India.
- xvi. Agency commission received by an agent of Life Insurance Corporation, Postal Savings, Unit Trust of India or other mutual funds if it is not his regular business.
- xvii. Commission received by a director for standing as guarantor.

- xviii. Commission received by a Director for under writing the shares of a new company.
- xix. Gratuity received by a non-employee director.
- xx. Any annuity or pension received from LIC or other insurer u/s 80CCC.

8.4 SPECIFIC INCOMES [SECTION 56(2)] :

1. Dividend

Income from all dividends is specifically included in this head. The shares may be held as stock-in-trade but any dividend received during the period when they are held by the assessee shall be exempted.

It can be received on equity or preference of a company, units of UTI or shares of a Cooperative Society. Following points are to be noted while treating dividend for tax purpose.

- Dividend declared or distributed by an Indian Company or by mutual funds on its units is fully exempted with effect from 1-4-2003.
- Bonus shares allotted to preference share holders shall be deemed as dividend and their market price shall be fully taxable.
- In case loan is taken by a person who has substantial interest in the affair of a Pvt. Ltd. Company whose business is not money lending, such loan is deemed as advanced dividend up to accumulated reserves of the company. If such loan is adjusted against-future dividend, it will not be taxable. A person is said to have a substantial interest if he, his spouse and minor child all together hold 10% or more shares in such Pvt. Ltd. company.
- Deemed dividend as per (b) and (c) above is fully taxable.

ILLUSTRATION – 1 :

'B' is a holder of 5,000 equity shares of ₹100 each (fully paid) in 'M' & Co. Ltd. on 1-1-2022 the company decided to issue to its equity shareholders bonus shares out of the balance in the General Reserve Account at the rate of one bonus share of ₹100 each (fully paid) for every five years held by them. On 31st March 2022, 'B' received 1,000 bonus shares from the company, the market value of the bonus share on that date being ₹120 per share. Discuss 'B's liability to tax in respect of the bonus shares received by him. Would your answer be any different if 'B' had received the bonus shares as a holder of a company's preference shares?

SOLUTION :

The issue of bonus shares out of capitalized accumulated profits does not entail the release of any asset and as such bonus shares are not dividend when they are issued to holders of equity and ordinary shares. Two conditions must be fulfilled to include the issue of bonus shares in category of dividend in the hands of the recipient shareholder. These conditions are:

- (a) Dividend must have been issued out of accumulated profit of the company.
- (b) It must entail the release of the assets of the company.

Since in the above issue of bonus shares to equity shareholders does not entail the release of the assets of the company, so this does not constitute dividend in the hands of the shareholder. But bonus shares distributed amongst the preference shareholders will amount to dividend.

Q.NO. – 1 :

Mr. D holds 2,000 preference shares of ₹100 each in a company. Company had reserves worth ₹50,00,000. Out of these reserves it issued bonus shares in the ratio of 1: 4. Market value of these shares amounts to ₹ 116/- per share. How will they be treated in the hands of Mr. D?

[Hints: u/s 2(22) to be treated as dividend- ₹ 58,000]

2. Winning from lotteries, crossword puzzles, races including horse races, card games and games of other sorts, or from gambling or betting of any form or nature [Section 56(2) (IV)].

This point can be split up in following parts :

- (a) Winning from lotteries;
- (b) Winning from cross word puzzles;
- (c) Winning from races including horse races;
- (d) Winning from card games;
- (e) Winning from games if of other sorts such as game shows or entertainment programmes on TV or other electronic media in which people compete to win prizes;
- (f) Winning from gambling and betting.

No expenditure is allowed to be deducted out of these incomes.

Tax is deducted at source at prescribed rates out of following incomes :

- | | |
|-------------------------------------|--------------------------|
| (a) Winnings from lotteries | If prize exceeds ₹ 5,000 |
| (b) Winnings from crossword puzzles | If prize exceeds ₹ 5,000 |
| (c) Winnings from card games | If prize exceeds ₹ 5,000 |
| (d) Winnings from T.V. game shows | If prize exceeds ₹ 5,000 |
| (e) Winnings from horse races | If prize exceeds ₹ 2,500 |

In case of Winnings from other races, gambling, betting etc --- No TDS

3. Amount deducted by employer :

Any amount deducted by an employer (not carrying on business or profession) as Income-tax, or E.S.I. Fund contribution or their contribution to provident fund etc. shall be treated as income of the year.

4. Interest on Securities :

The following amounts due to an assessee in the previous year shall be chargeable to income-tax under Interest on Securities :

- (i) Interest on any security of the Central or State Government.
- (ii) Interest on debentures or other securities for money issued by or on behalf of a local authority or a company or a corporation established by a Central, State or Provincial Act.[Section 2(28B)]

Interest is the return which a person receives from another person for bearing the risk of parting with the money and losing the income which he would have received on such money had he deposited it in a bank. It simply means the return received by a creditor who has given his money as debt.

A security is a document acknowledges the debt taken by a specific authority from general public. It may be named as a 'Debt' 'Loan', 'Paper', 'Debenture' or 'Security' or 'Certificate'. It is secured in some manner.

Contents of Security: It contains face value of security, date of maturity, rate of interest, date, place and period of payment of interest etc. These are transferable.

Who can issue a security? As per section 18, securities may be issued by following authorities :

- (i) The Central Government;
- (ii) A state Government;
- (iii) A Local Authority;
- (iv) A Company; or
- (v) A Statutory Corporation.

TYPES OF SECURITIES

A. Exempted from tax

Income-tax Act, 1961 provides for certain interest from tax u/s 10(15). Interest on all such securities, certificates, bonds etc. is altogether not included in the gross total income of the assessee and no tax is payable there upon.

There are some securities whose interest is exempted from tax but these are no longer in existence. These are:

- (i) National Plan Certificates;
- (ii) National Defence Bonds;
- (iii) Treasury saving deposit certificates;
- (iv) Special Bearer Bonds 1991.

Interest on following bonds issued by public sector Companies/undertakings has been notified to be exempted :

- (i) 10% Secured Redeemable NTPC Bonds, 1986 (1st Series).
- (ii) 10% Secured Redeemable non-convertible Bonds issued by Mahanagar Telephone Nigam Ltd.
- (iii) 10% Secured Redeemable non-convertible Bonds issued by Indian Railway Finance Corp. Ltd.
- (iv) 9% Secured Redeemable non-convertible Bonds 1987 (B Series) issued by National Hydro-electric Power Corp. Ltd.
- (v) 9% Secured Redeemable non-convertible Bonds issued by Indian Railway Finance Corp. Ltd.
- (vi) 9% (tax-free) Secured Redeemable Bonds issued by Power Finance Corp. Ltd.
- (vii) 10% (tax-free) Secured Redeemable non-convertible Bonds issued by Indian Telephone industries Ltd.
- (viii) 10 years – 9%(tax-free) Secured Redeemable non-convertible NTPC Bonds –IVth Issue (private placement)
- (ix) 10 years – 9%(tax-free) Secured Redeemable non-convertible PFC Bonds –II Series(private placement) issued by Power Finance Corp.
- (x) 10 years – 9%(tax-free) Secured Redeemable non-convertible REC Bonds, issued by Rural Electrification Corp. Ltd.
- (xi) 10 years – 9%(tax-free) Secured Redeemable non-convertible (C Series) issued by Neyveli Lignite Corp. Ltd.
- (xii) 7% Capital Investment Bonds.
- (xiii) 6.5%, 8%, 9% or 10% National Relief Bonds.

B. Tax free securities :

- (a) Tax-free Commercial (Non Govt.) Securities :** These securities are those which are issued by a local authority, statutory corporation or a company in the form of debentures or Bonds. Actually, these are not tax-free. Tax is paid by the issuing authority to the Government on behalf of such security-holders. The person who is holder of such security is liable to tax not only for the interest he is to receive but also

the amount of tax which has been deposited on his behalf. The amount of interest actually received by holder is the net interest, i.e., after deduction of tax at source. We have to find out the gross interest, i.e., before deduction of tax, to include it is the gross total income of assessee. It can be done in the following manner:

Grossing up = Net Interest received X (100/ (100-rate of tax))

ILLUSTRATION – 2 : Mr. X invested ₹1,00,000 in 8% tax-free debentures of a company. What will be his taxable interest for the previous year ending on 31-3-2022 if the rate of deduction of tax at source is @ 20.6% Interest accrues on 1st January every year.

SOLUTION :

Net Interest due = $1,00,000 \times (8/100) = ₹ 8,000$

Grossed up = $8,000 \times (100/(100-20.6)) = 8,000 \times (100/79.4) = ₹ 10,076$

Interest to be added in gross total income of Mr. X for the previous year ending on 31-3-2022 shall be ₹ 10,076.

(b) Tax free Govt. Securities : These securities are no longer existence. Now the word tax free written in Govt. securities is presumed to mean that interest on such securities is exempted u/s 10(15).

C. Less Tax Securities: This is the most common form of securities. Out of the amount of interest due to a security-holder, tax at the prescribed rates has to be deducted by the issuing authority before payment of interest. The assessee is to pay tax not only on the net amount of interest received, but he shall be liable to pay tax on gross interest i.e., amount due before deduction of tax at source. When the face value of securities and the rate of interest is given, it will be directly give us the gross interest which we shall include in his gross total income, e.g., ₹ 50,000, 6% port Trust Bonds. Gross interest due = 3,000. It shall be fully added in the Gross Total Income of such person.

Taxability of Interest :

- (i) Interest on securities accrues after a fixed period as mentioned on the face of the security itself. In India, generally, interest accrues after a period of six months. Any interest which accrues to a person during the previous year is added in his gross total income.
- (ii) Interest is taxable on due basis. It is immaterial whether the assessee has received it or not.
- (iii) The interest in securities issued by Govt. of India accrues in India even if they are enforced for payment outside India. [C.I.T. v. Bansi Lal Moti Lal]
- (iv) Interest accrues on the name of that person on whose name securities stand on the date of accrual of interest. It is immaterial that he purchased these securities a few days earlier than the date of accrual of interest. He has to include full interest in his gross total income.

- (v) Interest on securities does not accrue on day-to-day basis. It matures into debt overnight, i.e., the day of accrual of interest.

5. Amount received as gift to be treated as income: [Section 2(24)(xiii) and Section 56(2)(v)] :

Where any sum of money, the aggregate value of which exceeds ₹ 50,000 is received without consideration by an individual or HUF from any person or persons on or after 1-4-2007, the whole of such sum shall be deemed as income of the previous year in which it is received.

Provided that this clause shall not apply to any sum of money received :

- (a) From any relative; or
- (b) On the occasion of marriage of the individual; or
- (c) Under a will or by way of inheritance; or
- (d) In contemplation of death of the payer.
- (e) From any fund or foundation, a University or other educational institution or hospital or other medical institution or any trust or institution referred in Sec. 10(23C) or,
- (f) From any trust or institution registered u/s 12AA.

Explanation : For the purposes of this clause “relative” means

- (i) Spouse of the individual;
- (ii) Brother or sister of the individual;
- (iii) Brother or sister of the spouse of the individual;
- (iv) Brother or sister of either of the parents of the individual;
- (v) Any lineal ascendant or descendant of the individual;
- (vi) Any lineal ascendant or descendant of the spouse of the individual;
- (vii) Spouse of the person referred to in Clauses (ii) to (iii).

The above provisions can be explained in following manner :

Gift as taxable incomes :

Any amount received by an individual or HUF or is credited to their account on or after 1-4-2008 shall be deemed as income taxable under the head “Income from other sources”.

Gifts which are not to be treated as incomes :

Following amounts received without consideration shall not be considered as income:

- (i) The sum received before 1-4-2008

(ii) The sum received by any individual from a relative

The term “relative” means :

- (a) Spouse of the individual;
 - (b) Brother or sister of the individual;
 - (c) Brother or sister of the spouse of the individual;
 - (d) Brother or sister of either of the parents of the individual;
 - (e) Any lineal ascendant or descendant of the individual;
 - (f) Any lineal ascendant or descendant of the spouse of the individual;
 - (g) Spouse of the person referred to in Clauses (ii) to (iii).
- (iii) The sum received on the marriage of an individual; or
- (iv) The sum received by any individual or a Hindu undivided family under a will or by way of inheritance; or
- (v) Any sum received in contemplation of death of the payer; or
- (vi) Any number of gift or gifts received during the year provided the aggregate amount of all gifts does not exceed ₹ 50,000.
- (vii) Any sum of money received against consideration.

To conclude it can be said that the aggregate amount of gift or gifts from all non-relatives if exceeds ₹ 50,000 in any previous year, it is taxable in the hands of the recipient of such gifts.

ILLUSTRATION – 3 :

Mr. Krishna received the following gifts during the previous year 2021-22. Compute his taxable income under the head ‘Income from Other Sources’:

- a. Received ₹ 1, 00, 000 as gift from a friend on 1-6-2021;
- b. Received a Microwave costing ₹ 14, 500 as gift from his another friend;
- c. Received ₹ 50, 000 as a gift from another friend on 1.11.2021;
- d. Received ₹ 30, 000 as gift from his sister on 1.1.2022;
- e. Received ₹ 40, 000 as gift from his friend Mr. Hari on 1.12.2021;
- f. Received ₹ 1, 60, 000 as gift from his non-resident friend on 1.2.2022.

SOLUTION :

Computation of Income from Other Sources

Gift	Treatment	₹
Gift from a friend on 1.6.2021	Taxable	1, 00, 000
Gift from another friend on 1.11.2021	Taxable	50, 000
Gift from his sister on 1.1.2022	gift from a relative is exempted	NIL

Income Tax	8.11	Income from Other Sources
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Gift from his friend Mr. Hari on 1.12.2021	Taxable	40,000
Gift from his non-resident friend received On 1.2.2022	Taxable	1,60,000
Gift of Microwave	Exempted as in-kind	NIL

Total taxable gifts		3,50,000

Aggregate amount of gifts from all non-relatives is taxable if the total amount of such gifts exceeds ₹ 50,000 in any previous year.

6. Income from letting of plant, machinery or furniture : If an assessee owns plant, machinery or furniture and it is let out to some other person, the rent so received by the assessee shall be chargeable to tax under this head provided letting of plant and machinery is not the business of the assessee.

If the assessee is engaged in the business of letting out plant, machinery or furniture, the rent so received shall be chargeable to tax under the head 'Profits and Gains of Business or Profession'.

7. Income from letting of plant, machinery or furniture : The rent from a property is taxable under the head 'Income from House property' but when an assessee lets out plant, machinery or furniture which is inseparable from building, the rent of building so received will be taxable under the head 'income from Other Sources'. The letting of plant, machinery or furniture should not be the business of the assessee.

8. Any sum received under a Keyman Insurance Policy including any sum allocated by way of bonus [u/s 2(24) (xi)] if such amount is not taxable under the head "Profits and Gains of Business and Profession" or under the head "Salaries".

8.5 DEDUCTIONS ALLOWED [SECTION 57] :

The taxable income under the head 'income from other sources' shall be computed after allowing deductions as provided in section 57 :

1. **In case of Dividends and Interest on Securities :** From the dividend income, a deduction shall be allowed in respect of any sum spent by way of commission or remuneration to a banker or any other person as collection charges for realizing the dividend or Interest on Securities.
2. **Repairs, depreciation, etc. in case of letting of machinery, plant or furniture with or without building :** The following deductions shall be allowed from the income earned by letting of machinery, plant or furniture with or without building.
 - (a) Expenditure incurred on current repairs of plant, machinery, furniture or building.
 - (b) Insurance premium paid regarding these assets.

- (c) Depreciation on plant, machinery and furniture, Depreciation in respect of buildings will be allowed only if the assessee is the owner. It will not be allowed if the assessee is lessee or mortgagee in possession of the building.

3. Deduction in respect of employee's contribution in staff welfare schemes [57 (IA)]. Any amount received by employer from his employees as their contribution of provident fund, E.S.I. Fund or superannuation fund is deemed as income u/s 59(ic) if not taxable under the head "Profits and Gains of Business and Profession".

In case employer deposits any amount (out of these incomes) in these funds before prescribed due date, such amount is allowed as deduction u/s 57(ia)

4. Standard Deduction out of Family Pension [Section 57(ia)] : In case of income in the nature of family pension, a deduction of a sum equal to 33 1/3 of such pension or ₹ 15,000 whichever is less, shall be allowed.

Family pension means a regular monthly amount payable by employer to the legal heirs of deceased employee.

5. Deduction from any other income [Section 57(iii)] : Any expenditure which is spent to earn an income chargeable to tax under this head shall be deducted from such income. This deduction is not admissible to assessee being a foreign company.

The assessee, M/s. Lakshmi Agents Pvt. Ltd., Jamanagar, was doing agency business. The assessee borrowed money which was invested to purchase shares of a company which was managed by M/s. Lakshmi Agents Pvt. Ltd. The Gujarat High Court decided in the case of Lakshmi Agents Pvt. Ltd. Vs. The Additional Commissioner of Income Tax that since the money was borrowed to purchase shares, so the interest paid on borrowed money shall be allowed to as deduction out of dividend income, i.e., it is an allowed deduction of "Income from Other Sources". The interest paid on borrowed money cannot be charged against the business income of the assessee.

To claim this deduction following conditions must be satisfied :

- (a) The expenditure should be incurred solely for earning such income.
- (b) It should not be in the nature of capital expenditure.
- (c) It should not be in the nature of personal expense.
- (d) It should be incurred in the relevant accounting year.

6. Deduction form royalties received by authors (other than those writing for films) Actual expenses can be claimed as deduction.

8.6 DEDUCTION NOT ALLOWABLE [SECTION 58] :

The following expenses are not allowed to be deducted from such income:

In case of any Assessee –

- (i) Any personal expenses of the assessee.

- (ii) Any interest chargeable under this Act which is payable outside India on which tax has not been paid or deducted at source.
- (iii) Any payment which is chargeable under the head 'Salaries' if it is payable outside India unless tax has been paid or deducted at source.
- (iv) In case an assessee has income 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, such assessee shall not be allowed any deduction in respect of any expenditure or allowance in connection with such incomes.

In case of every assessee any payment to relatives and associates made in cash may be not allowed under section 40A in certain circumstances. The provisions of section 40A are made applicable under this head also by sub-section 2 of section 58.

ILLUSTRATION – 4 :

Mr. Rohan has the following incomes during the year ending 31.03.2023.

1. Dividend declared by Ravi Co. on 31.03.2021 ₹ 26, 000
2. Dividend declared by Vinay Co. on 31.03.2022 ₹ 29, 000
3. Interim dividend received on 1.5. 2021 ₹ 23, 000
4. He won gold worth ₹ 10, 00, 000 from Punjab state lottery
5. During March 2023 he earned ₹ 1, 00, 000 as prize money on horse races. These horses are owned by him and expenditure incurred on maintenance of these horses amounted to ₹ 1, 60, 000.

Compute from other sources for the assessment year 2022-23

SOLUTION :

Computation of Income from Other Sources

Dividend		₹
a. Declared by Ravi. Co. on 31.03.2021 [Not income of 2021-22]		NIL
b. Declared by Vinay. Co. on 31.03.2022 Exempted		NIL
c. Interim dividend received on 01.05 .2021 Exempted		NIL
Winning from Lottery		
Gold from Punjab State Lottery		10, 00, 000
Prize money of race horses	1, 00, 000	
Less: expenses on maintenance of these horses	1, 60, 000	

Less: to be carry forward	60, 000	NIL
-----		-----
Income from Other Sources		10, 00, 000

Q.No. 2

Compute income from other sources from particulars given below:	₹
1. Interest on deposits with a company	10, 000
2. University remuneration for working as examiner	6, 000
3. Royalty for writing books	60, 000
[He claims to have spent ₹ 20, 000 on writing these books]	
4. Dividend declared by X. Co. on 01.03. 2022 but paid on 01.05.2022	6, 000
5. Interim dividend paid on 01. 05 2021	3, 000
6. Stake money on race horses	1, 50, 000
Horses are maintained by him and expenses on maintenance of these	
Horses are	
	2, 40, 000
7. Family pension received	36, 000

8.7 PROFITS CHARGEABLE TO TAX [SECTION 59] :

Under section 59 (i) the provisions of sub-section (1) of section 41 have been made applicable in computing the income of an assessee under section 56 as they are applicable in computing the income under the head 'Profit and Gains of Business or Profession'.

This provision deals with any allowance or deduction which has been allowed under this head in the assessment of income in any earlier year in respect of any expenditure, loss or trading liability incurred by the assessee subsequently during any previous year, the same amount if it is received or recovered in cash or in any other manner shall be deemed to be the income of that previous year in which it is recovered irrespective of the fact whether the source of income continues to exist in that year or not.

8.8 METHOD OF ACCOUNTING [SECTION 145] :

Income taxable under the head 'Profits and Gains of Business or Profession' or under 'Income from Other Sources' has to be computed in accordance with the cash or mercantile system of accounting regularly employed by the assessee.

The Central Government has assumed the power to notify the various accounting standards to be followed by any class of assessee or in respect of any class of incomes.

In case assessing officer is not satisfied about the correctness or completeness of the accounts of the assessee, or assessee has failed to follow the method of accounting or has not followed the accounting standards as notified, the Assessing Officer may proceed to make best judgment assessment.

8.9 SUMMARY :

Any income which is to be included in total income but does not find place under any other head of income, is taxable under the head 'Income from Other Sources'. It includes dividends, income from winnings from lotteries, crossword puzzles, horse races, card games or betting etc., interest on securities, income from letting of machinery, plant or furniture which is not chargeable as business income, etc. In case of dividends or interest on securities,

any commission paid to a banker or any other person for collecting the dividends or interest on behalf of the assessee is deductible from such income. In the case of income from family pension received by the widows or heirs of deceased employee, deduction of sum equal to 33.3% of such income or ₹ 15,000, whichever is less, is to be allowed. Any security issued by the Central or State Government or local authority or any company or statutory corporation is a security for this purpose. Any interest earned on such securities is taxable under the head 'Other Sources', generally, on due basis.

8.10 KEY WORDS :

AOP	:	An Association of Persons
BOI	:	A Body of Individual
DDT	:	Dividend Distribution Tax
ESOP	:	Employee Stock Ownership Plan
TDS	:	Tax Deducted at Source
HUF	:	Hindu Undivided Family
LLP	:	Limited Liability Partnerships

RFCTLAR Act 2013 :

Right to Fair Compensation and Transparency in Land Acquisition, Rehabilitation and Resettlement Act, 2013

Dividends :

It is the sum paid to or received by a shareholder proportionate to his shareholding in a company out of the total sum distributed.

Dividend from a Foreign Company :

Dividends received from any foreign company are subject to taxation under 'Income from Other Sources'.

One-time Income :

One-time incomes such as winnings from lotteries, horse races, crossword puzzles, card games, gambling or betting of any form are categorized under 'Income from Other Sources.'

STT	:	Subject Transaction Tax
ULIP	:	Unit-Linked Insurance Plan
WDV	:	Written-Down Value

8.11 SELF ASSESSMENT QUESTIONS :

1. Define the term 'Dividend' as given in section 2(22) of Income-tax Act, 1961. How is the dividend income put to tax under the provisions of this Act?

2. Mention the different kinds of incomes specifically mentioned as chargeable to tax under the head 'Income from Other Sources'.
3. Enumerate the items of deductions allowable in computing income from other sources.
4. Discuss the various kinds of Securities? Explain the rule regarding grossing up of interest on Commercial Securities.
5. In July, 2021, Mr. Giri employed as marketing manager in a pharmacy company, received a Maruti car as gift from a distributor of the company. The value of the gifted car is estimated ₹ 2, 60, 000. Is the value of car taxable as income? If so, under which head is it taxable?

8.12 SUGGESTED READINGS :

1. V.P.Gaur and D.R.Narang, 'Income Tax Law and Practice', Kalyani Publication House, New Delhi
2. Mahendra B. Gabhawala, 'Direct Tax Ready Reckoner with Planning', Bharat Law House Pvt. Ltd., 2019.
3. Dr Vinod K.Singhania and Dr Kapil Singhania, 'Direct Taxes Law and Practice', Taxmann, 2023.
4. Dr Girish Ahuja and Dr Ravi Gupta, 'Direct Tax Ready Reckoner with Planning', Commercial Law Publisher (India) Pvt. Ltd., 2023.
5. Income tax act, Bharat Law House Pvt. Ltd.

Dr. Vishnu Vadde

Lesson – 9
DEDUCTIONS U/S – 80

Objectives :

After studying this lesson, you should be able to

- understand various deductions available from Gross Total Income
- calculate the amount of each deduction; and
- compute the taxable income of an assessee after allowing such deductions.

Structure of the lesson:

- 9.1 Meaning of Gross Total Income
- 9.2 Objectives of Providing Deductions
- 9.3 Important Points regarding Deductions
- 9.4 General Provisions
- 9.5 Deductions in Respect of Payments
- 9.6 Summary
- 9.7 Key Words
- 9.8 Self Assessment Questions / Illustrations
- 9.9 Suggested Readings

9.1 MEANING OF GROSS TOTAL INCOME :

Aggregation of taxable income computed under all heads of income is known as Gross Total Income. Gross Total Income of an assessee is that income from which the deductions of Section 80 have not yet been deducted. In other words, the income, before deducting all deductions U/s-80c to 80U of Income-Tax Act, is called Gross Total Income.

Clarifications :

- (1) It is not necessary that an assessee must have income from all heads of income. He may have income from all heads or few of them. In this case gross total income is an aggregation of such heads having income.
- (2) Gross Total Income does not only mean to aggregate of taxable income computed under each head of income. It is also helpful in giving effect to the provisions of set-off and carry forward of losses and clubbing of income. If there is no requirement in the question relating to clubbing of income and set-off of losses, in this situation the total of taxable income under each head of income shall be regarded as Gross Total Income.

Maximum Limit of Deductions – U/S-80 : Total deduction cannot be more than the gross total income (excluding long-term capital gain, short-term capital gain U/s-111A, winnings from lottery and races and income mentioned U/s-115A, 115AB, 115AC, 115ACA, 115AD, 115BBA, and 115D) of an assessee. If the total of all deductions exceeds the gross total income, the deductions shall be restricted to the extent of gross total income. In this case taxable income will be nil. The income can never be negative on account of such deductions. **In simple words, if there is no gross total income at all, no deduction U/s-80 shall be allowed.**

9.2 OBJECTIVES OF PROVIDING DEDUCTIONS :

1. Computation of Net Taxable Income.
2. Encouragement to Saving and Promoting Industries.
3. Earning of Foreign Exchange Reserves.
4. To promote feeling donation to charitable and religious institutions.
5. Reducing Tax Liability.
6. Gaining Tax planning objectives.

9.3 IMPORTANT POINTS REGARDING DEDUCTIONS :

1. Deductions should be claimed by the assessee.
2. It is the duty of the assess to disclose important facts regarding deductions.
3. Deductions are deducted before computing taxable income.
4. Amount of all deductions cannot exceed gross total income.

9.4 GENERAL PROVISIONS :

- A. Section 80A (1):** According to Section 80A (1), while computing the total income of an assessee, the deductions specified in Section 80C to 80U shall be allowed from the Gross Total Income of the assessee.
- B. Section 80A (2):** The aggregate amount of deduction specified in this section shall not exceed the Gross Total Income of the assessee in any case.
- C. Section 80A (3):** In case of AOP/BOI, if there is any deduction chargeable under Section 80G / 80GGC / 80-IA / 80-IB / 80-IC / 80-ID / 80- IE, no such deduction will then be made while computing the total income of the AOP/BOI in relation to their share in the income of the AOP/BOI.

9.5 DEDUCTIONS IN RESPECT OF PAYMENTS :

9.5.1 Deductions in respect of investments in specified assets [Section 80C] :

A. Deductions in respect of Investments / Contributions :

Under this Section, deduction can be claimed up to Rs.1,50,000 from gross total

income on savings in specified modes of investments. This deduction is only for individuals and HUF.

Following are the investments that are eligible for deduction under this section-

1. **Premium paid in respect of life insurance policy :**

Any premium paid on life insurance policy of spouse, parents, child (minor or major) and any member, in case of HUF is eligible for deduction under Section 80C. Insurance policies may include life insurance policy and endowment policy.

Exemption on receipts from LIC Section 10(10D)- any sum received from a life insurance policy or by way of bonus on such policy will not be included in the total income of the assessee.

2. **Premium paid in respect of a contract for deferred annuity :**

Any premium paid to keep in effect a contract for deferred annuity on the life of the assessee and/or his or her child, spouse given that the contract does not contain any provision for exercise of an option by the insured to receive cash on the payment of the annuity.

The contract of deferred annuity can be with any person.

3. **Any sum deducted from the salary payable of a government employee for securing a deferred annuity :**

Any sum deducted by or on behalf of government from the salary of a government employee for the purpose of securing a deferred annuity or making provisions for his spouse or children. The sum deducted should not exceed one fifth of his/her income

4. **Contribution to SPF/PPF/RPF:** Contributions to any provident fund under Provident Fund Act, 1925 and any recognised provident fund is eligible for deduction under Section 80C. Any other contribution to provident funds setup by the government under Public Provident Fund Scheme, 1968 also qualifies for the same deduction.

5. Contribution to approved superannuation fund.

6. Any sum paid/deposited in Sukanya Samriddhi Account.

7. Subscription to National Savings Certificate VIII.

8. Contribution to unit linked insurance plan 1971.

9. Contribution to unit linked insurance plan of LIC Mutual Fund.

10. Contribution to approved annuity plan of LIC.

11. Subscription towards notified units of mutual fund or UTI.

12. Contribution to notified pension fund set up by mutual fund or UTI.

13. Contribution to national housing bank (Tax saving) Term Deposit Scheme, 2008.
14. Subscription to notified deposit scheme.
15. Payment of tuition fees to any university, college, school or any other educational institutions within India for full time education for maximum 2 children.
16. Repayment of housing loan including stamp duty, registration fee and other expenses.
17. Subscription to certain equity shares or debentures.
18. Subscription to certain units of mutual fund.
19. Investment in five-year term deposit.
20. Subscription to notified bonds issued by NABARD.
21. Investment in five-year Post-Office time deposit.
22. Deposits in Senior Citizen Savings Schemes Rules, 2004.

B. Termination of insurance policy or unit linked insurance plan or transfer of house property or withdrawal of deposit :

Where in any previous year an assessee ;

- a. Terminates his/her contract of insurance by giving notice which would affect or where the contract ends to be in force.
- b. Terminates his/her involvement in any Unit Linked Insurance Plan by giving notice that would affect or where he stops to participate because of failure to pay any contribution.
- c. Transferring the house property before the expiry of five years from the end of the financial year in which possession of the property is acquired by him, or receives back, whether by way of refund or by any sum.

Then, no such deduction would be allowed to the assessee in respect of any sum paid during that previous year.

9.5.2 Deduction in respect of Contribution to certain Pension Funds [Section 80CCC] :

In case of an assessee in the previous year has paid or deposited any amount out of his income which is chargeable to tax to keep in force any annuity plan of LIC or any other insurer for receiving pension from the fund set up by them, he/she shall be allowed a deduction in the computation of his total income.

The maximum amount of deduction permissible is Rs. 1,50,000. However, the amount of deduction mentioned here is **clubbed with 80C and 80CCD (1)**.

9.5.3 Deduction in respect of contribution to Pension Scheme notified by the Central Government [80CCD] :

Contribution made towards notified pension schemes by Central Government i.e. New Pension Scheme (NPS) are allowed deduction U/s- 80CCD on individual.

In exercise of the powers conferred by section 80CCD (1), the Central Government has notified the 'Atal Pension Yojana (APY)' as a pension scheme, contribution to which would qualify for deduction under section 80CCD in the hands of the individual.

According to the **Restructured Defined Contribution Pension System** people entering newly to Government service on or after 1 January, 2004 should contribute 10% of their salary to pension account monthly. Equivalent amount is also contributed by government to such account. Benefits of this account are also available to individuals employed by other individuals or self employed individuals.

Section 80CCD (1) provides a deduction on the amount paid or deposited being 10% of his/her salary in the pension account. The deduction for self-employed individual would be 20% of his/her Gross Total Income.

Section 80CCD (1B) provides for additional deduction up to Rs. 50,000 for the amount that they deposit in the National Pension Scheme.

Section 80CCD (2) provides for additional deduction for their contribution to employee's pension account upto 10% of their salary.

Limit on deduction under Sections 80C, 80CCC & 80CCD(1) [Section 80CCE]

Under the Section 80C, 80CCC, 80CCD(1) the maximum amount of deduction is restricted to Rs. 1,50,000. Also, the additional deduction provided in Sec 80CCD(1B) and 80CCD(2) would be beyond the limit of Rs. 1,50,000.

9.5.4 Deduction in respect of investment made under an equity savings scheme [Section 80CCG] :

Under this Section deduction is available to resident individuals whose Gross Total Income is up to Rs.12 lakhs and upon the fulfilment of the following conditions-

- A. Should be a retail investor under the requirements of the scheme notified.
- B. Investment should be made in listed equity shares or listed units of equity-oriented fund.
- C. Minimum lock in period should be 3 years from the date of acquisition

The deduction upon the fulfilment of the above conditions would be least of the following -

- a. 50% of the amount is invested in equity shares; or
- b. Rs. 25,000 for 3 Assessment Years.

If an assessee after claiming the deduction fails to comply with any of the

above conditions in the previous year than the amount of claim would be deemed to be income and accordingly be charged for tax.

The Rajiv Gandhi equity savings scheme has been discontinued from 1 April 2017 so no deduction would be available from AY 2018-19.

But if an assessee has invested any amount before AY 2017-18 then he/she shall be allowed deduction until AY 2019-20.

9.5.5 Deduction in respect of Medical Insurance Premium [Section 80D] Individuals :

- Deduction up to Rs. 25,000 for payment of premium to keep in force any health insurance policy of self, spouse and children or contribution made Central Government health scheme, or such other health scheme as notified by Central Government.
- Further deduction up to Rs. 25,000 is allowed when payments are made to keep in force any health insurance policy of parents and in respect of health check-ups of parents.
- The deduction of Rs. 25,000 can extend up to Rs. 30,000 if any person mentioned is of age 60 years & above and 80 years & above at any time during the relevant previous year.
- Again, if payments are made in the following situations and ways, then only the claims under Section 80D can be made-
 - By any mode (**including cash**) on account of any sum paid for health check-ups;
 - By any mode (**other than cash**) in all cases.

HUF :

- Premium paid on the health insurance of any member of the family is allowed as deduction under Section 80D.
- Maximum deduction under this section in Rs. 25,000 and in case the member is senior citizen then the amount would be Rs. 30,000.
- Any amount paid on medical expenditure of such member who is very senior citizen i.e. 80 years or more would be allowed a deduction Rs. 30,000 given no amount has been paid on the health insurance of the person.

Other conditions :

- The premium should be paid out of the income chargeable to tax in any mode other than cash, in the previous year.
- The insurance should be in accordance with the schemes made by, GIC of India and approved by Central Government; or any other insurer approved by IRDA.

9.5.6 Deduction in respect of maintenance including medical treatment of a Dependent Disabled [Section 80DD] :

The deduction under this section applies to individual or HUF being a citizen of India.

Deduction can relate to -

- Any amount incurred for medical treatment, training or rehabilitation of a dependent being a person with disability, or
- Any amount paid/deposited under any scheme framed by LIC or any other insurer/administrator/specified co. as referred in UTI Act, 2002, for the maintenance of a person with disability being dependent on the assessee.

The deduction allowed is Rs. 75,000 and in case of severe disability i.e. person with 80% or more is Rs. 1,25,000.

If the dependent with disability dies before the individual in whose subscription was made, then the amount paid or deposited would be chargeable in the hands of assessee under that particular scheme in the PY in which the amount is received by the assessee.

9.5.7 Deduction in respect of Medical Treatment, etc. [Section 80DDB] :

- **Eligibility of the assessee :**

Under this section deductions are allowed to any individual or HUF in respect of medical treatment of self or a dependent being a resident of India, who is suffering from a specified disease.

- **Amount of deduction :**

- **For individuals and HUF below age 60**

Least of the following is available as deduction with respect to any expenses made towards treatment of specific disease for himself or any of his dependents.

- Amount actually paid; or
- Rs. 40,000.

For HUF, such a deduction is available to any of the HUF members.

- **For senior citizen or an individual of age 60 or more**

Amount paid at any time during the relevant PY in respect of a senior citizen or for himself, then least of the following will be allowed as deduction-

- Amount actually paid; or
- Rs. 60,000

- **For very senior citizen or an individual of age 80 or more**

Amount paid at any time during the relevant PY in respect of a very senior citizen or for himself, then least of the following will be allowed as deduction-

- Amount actually paid; or
- Rs. 80,000

In case, the sum of money is received from any insurance company under any insurance policy on health of the dependent or any sum reimbursed from an employer than such insurance or reimbursement received shall be excluded from the deduction.

- **Condition for the allowance of such claim**

Unless the assessee obtains the prescription for such medical treatment, no such deduction shall be allowed.

9.5.8 Deduction in respect of interest Loan taken Higher Education [Section 80E]

- **Eligibility and conditions :**

Deduction under Section 80E is allowed to an individual in respect of any interest on loan taken for the purpose of his/her or for his/her relatives paid by him in the previous year out of his income chargeable to tax. The loan must be taken from any financial institution or approved charitable institution.

- **Deduction period :**

Deduction is allowed in computing the total income. The earlier of the following would be considered -

- The initial AY and seven AY immediately succeeding the initial AY; or
- Until the interest is in full by the assessee.

- **Financial institution – it means**

- A banking company under Banking Regulation Act, 1949
- Any other institution as specified by Central Government in the official gazette.

9.5.9 Deduction for interest on Home Loan [Section 80EE] :

The Section 80EE stipulates deduction for interest paid on loan borrowed for acquiring self-occupied house by an individual until the complete repayment of the loan is not done. The maximum deduction available under this section is Rs. 50,000. However, this amount is over and above the limit mentioned in Section 24 on this behalf.

Conditions to be fulfilled to claim such deduction are :

- Assessee should not possess any residential house on the date of sanctioning of the loan,
- Value of the house should be Rs. 50 lakhs or more,
- The loan should get sanctioned during P.Y. 2016-17, and
- Sanctioned loan should be Rs. 35 lakhs or more.

9.5.10 Deduction in respect of donation to certain Funds, Charitable Institutions, etc. [Section 80G] :

Deductions are available in respect of donations to certain funds, charitable institutions, etc.

These deductions are divided into 4 categories which are follows :

1. Donations qualifying for 100% deductions, without anyqualifying limit

- National Sports Fund
- National Cultural Fund
- Fund for Technology Development and Application
- National Children's Fund
- Chief Minister's Relief Fund or Lieutenant Governor's Relief Fund with respect to any State or Union Territory
- The Army Central Welfare Fund or the Indian Naval Benevolent Fund or the Air Force Central Welfare Fund, Andhra Pradesh Chief Minister's Cyclone Relief Fund, 1996
- The Maharashtra Chief Minister's Relief Fund during
- October 1, 1993 and October 6, 1993
- Chief Minister's Earthquake Relief Fund, Maharashtra
- Any fund set up by the State Government of Gujarat exclusively for providing relief to the victims of earthquake in Gujarat
- Any trust, institution or fund to which Section 80G(5C) applies for providing relief to the victims of earthquake in Gujarat (contribution made during January 26, 2001 and September 30, 2001) or
- Prime Minister's Armenia Earthquake Relief Fund
- Africa (Public Contributions — India) Fund
- Swachh Bharat Kosh (applicable from financial year 2014-15)
- Clean Ganga Fund (applicable from financial year 2014- 15)
- National Fund for Control of Drug Abuse (applicable from financial year 2015-16)
- National Defence Fund set up by the Central Government
- Prime Minister's National Relief Fund
- National Foundation for Communal Harmony
- An approved university/educational institution of National eminence

- Zila Saksharta Samiti constituted in any district under the chairmanship of the Collector of that district
- Fund set up by a State Government for the medical relief to the poor
- National Illness Assistance Fund
- National Blood Transfusion Council or to any State Blood Transfusion Council
- National Trust for Welfare of Persons with Autism, Cerebral Palsy, Mental Retardation and Multiple Disabilities

2. Donations qualifying for 50% deductions, without any qualifying limit

- The Jawaharlal Nehru Memorial Fund
- Prime Minister's Drought Relief Fund
- Indira Gandhi Memorial Trust
- Rajiv Gandhi Foundation

3. Donations qualifying for 100% deductions, subject to a qualifying limit of 10% of adjusted Gross Total Income

- Government or any approved local authority, institution or association to be utilized for the purpose of promoting family planning.
- Donation by a Company to the Indian Olympic Association or to any other notified association or institution established in India for the development of infrastructure for sports and games in India or the sponsorship of sports and games in India.

4. Donations qualifying for 50% deductions, subject to a qualifying limit of 10% of adjusted Gross Total Income

- Any Institution or Fund established in India for charitable purposes fulfilling prescribed conditions.
- The Government or any local authority for utilisation for any charitable purpose other than the purpose of promoting family planning.
- An authority constituted in India by or under any other law enacted either for dealing with and satisfying the need for housing accommodation or for the purpose of planning, development or improvement of cities, towns and villages, or both.
- Any Corporation established by the Central Government or any State Government for promoting the interests of the members of a minority community.

- for renovation or repair of Notified temple, mosque, gurdwara, church or other place of historic, archaeological or artistic importance or which is a place of public worship of renown throughout any State or States.

Adjusted Gross Total Income means Gross total income less the following :

- (i) amount of deduction under Section 80C to 80U excluding 80G
- (ii) any income chargeable to tax
- (iii) Long Term Capital Gains under Section 112 Short Term Capital Gains under Section 111A.

Other conditions that needs to satisfy are-

- (i) If deduction is claimed and received on any amount under this section than no other deduction on the same can be claimed for the same or any other AY under any provisions of the act.
- (ii) Donations in kind are shall not qualify for deduction.
- (iii) Donations exceeding Rs. 2000 shall not qualify for such deduction unless paid by any mode other than cash.
- (iv) The deduction under this section can be claimed whether it has any relation with the business or not.

9.5.11 Deduction in respect of Payment of House Rent [Section 80GG] :

This section provides deduction on the amount of rent paid by the assessee upon the fulfilment of the following conditions :

- A. The assessee should not be receiving any HRA exempt under Section 10(13A).
- B. The rent paid on any accommodation should exceed 10% of his total income after all the deductions mentioned in Chapter VI A except 80GG.
- C. The accommodation should be occupied by the assessee for his/her own residence.
- D. The assessee or his spouse/children or the HUF of which he might be a member should not own any residence at the place where he/she is carrying the business & profession or employment or perform duties.

9.5.12 Deduction in respect of donations for Scientific Research and Rural Development [Section 80GGA] :

Under Section 80GGA deduction is available for donations for scientific research and rural development for an assessee not having income under “Profits and Gains from business and profession”.

The following donations are qualified for deduction :

- 1) Any payment made in the PY towards research institutions or college/university for scientific research as the main objective from such donations.
- 2) Any sum paid towards an association or any institution for taking up rural development programme as main objective as approved by the prescribed authority or to an institution or association for training of persons for taking up any rural development programme.
- 3) Any sum paid to research associations, university for taking up research in social sciences or statistics.
- 4) Such Research Association, University, College or institution must be approved under section 35(1)(iii).
- 5) Any fund paid rural development fund set up and notified under Section 35CCA.

However, restrictions are provided while claiming the deduction as follows -

- (i) If deductions under this section are already claimed on any amount than no other deductions can be claimed under any provisions of the act on such amount.
- (ii) No deduction shall be made for any amount exceeding Rs. 10,000 unless the amount is paid by any mode other than cash.

9.5.13 Deduction in respect of contributions given to Political Parties [Section 80GGB] :

Deduction under Section 80GGB is available for contributions made towards political parties or electoral trusts by companies in the previous year.

However, no deduction shall be allowed in case of payment made by cash.

The meaning of **Contribution** for this purpose is same as given by Companies Act, 1956-

- (i) Any donation or subscription or payment made towards a person by a company for carrying on any activities which are probably to affect the support of public for a political party shall also be defined to be a contribution for a political purpose;
- (ii) The expenditure incurred by a company on advertisement in any publication by/on behalf of a political party or for its advantage shall also be considered as a contribution to the political party or a contribution for a political purpose to the person publishing it.

9.5.14 Deduction in respect of contributions given by any person to Political Parties [Section 80GGC] :

- The Section 80GGC provides deduction for any sum contributed towards a political party or an electoral trust in the previous year by any person.

However, no such deduction would be allowed for any sum contributed by way of cash.

- This deduction will not be available to a local authority and an artificial juridical person, wholly or partly funded by the Government.
- **Political party in such case** means a political party registered under section 29A of the **Representation of the People Act, 1951**.

9.5.15 Deduction in Respect of Profits from Undertakings of Enterprise Engaged in Infrastructure Development (Section 80 IA) :

This deduction is allowed to those assesseees whose income includes the profits of the following type of enterprises like Telecommunication Services, Infrastructure Facilities, Industrial Park and Generation and Distribution of Power. This deduction is allowed in respect of profits and gains derived from any business of

a) Infrastructure Facility :

It means

- i) A road, bridge, rail system.
- ii) A highway project including housing.
- iii) A water supply project, irrigation project, sanitation and sewerage system of waste management system, and
- iv) A port, airport, inland waterways or inland port.

This deduction will be allowed subject to the following conditions :

- i) It starts operating and maintaining the infrastructure facility on or after 1st April, 1995 but upto 31st March, 2017.
- ii) It enters into an agreement with the Central or State Government for development, maintenance and operation of new infrastructure facility.
- iii) It is owned by a company registered in India or by an authority or a board or a corporation or any other body established or constituted under any central/state act.

b) Telecommunication Services :

Any undertaking starts providing telecommunication services after 31.03.1995 but before 1.4.2005. Both basic and cellular including radio, paging, domestic satellite services or network of trucking, broadband network and internet services and electronic data interchange services are included in telecommunication services.

c) Industrial Park :

Any undertaking develops, maintains and operates an industrial park or Special Economic Zone (notified by Central Government) after 31.03.1997 but before 1.4.2006 (for

Special Economic Zones) and operation of industrial parks must start between April 1, 2006 and March 31, 2011.

d) Generation and Distribution of Power :

An undertaking which is set up in any part of India for

- i) Generation and distribution of power after 31.03.1993 and ending on 31.03.2017.
- ii) Starts transmission or distribution by laying a network of new transmission. Or Distribution lines after 31.03.1999 but before 01.04.2017.

e) Businesses involved in the Distribution of Natural Gas :

If a cross-country natural gas distribution network (including laying of pipe lines and storage facilities). Operations are carried out subject to certain conditions deduction is allowed under this Section.

Quantum and period of deduction

- a) Telecommunication Services
 - i) First ten assessment years – 100% of profits.
 - ii) Next five assessment years – 30% of such profits for the total of 15 years from the year of its commencement.
- b) Others – 100% of such profits for 10 consecutive assessments year (out of 15 years) beginning with year in which it becomes operational. However, except in case of inland water ways, inland ports or navigational channel in the sea, the period shall be 20 years in place of 15 years.

9.5.16 Deduction in Respect of Profits from Industrial Undertaking, other than Infrastructure Development Undertakings (Section 80 IB) :

This deduction is allowed to those assesseees whose total income in respect of profits derived by different undertakings from any business of scientific and industrial research, construction and development of housing projects, maintaining, storing and transportation of food grains, refining of mineral oil, operating and maintaining hospitals in rural areas, an industrial undertaking including institution engaged in cold chain facility, multiplex theatres, business of hotel, convention centres.

This Section applies upon those enterprises established in India which are not engaged in the production of the articles or commodities mentioned in eleventh schedule of Income Tax Act.

These enterprises should not be formed by old business. The old machine should not be more than 20% of total cost.

If the industrial undertakings are established in backward states and commences production during the period from 1.4.1993 to 31.3.2004 (31.3.2012, in case of Jammu & Kashmir) deductions shall be allowed as under:

- (i) Company – 100% for first 5 years, 30% for next 5 years.
- (ii) Co-operative Society - 100% for first 5 years, 25% for next 7 years.
- (iii) Other – 100% first 5 years, 25% for next 5 years.

I. **In case of Scientific Industrial Research and Development [Section 80 IB (8)]:** This deduction is allowed to a company registered in India and it should be approved for the time being, prior to 1.4.1999 by the prescribed authority at any time. This deduction shall be allowed from the assessment year 1997-98. 100% deduction from profits shall be allowed for 5 consecutive years and if the enterprise is approved by the prescribed authority after 31.03.2000 but before 1.4.2007, then this deduction shall be allowed for 10 years started from initial year.

II. **In case of refining of mineral oil [Section 80 IB(9)]:** If the enterprises are established in north-east region, it has started its production on mineral oil before 1.4.1997 and if the enterprises are established in other states and started the production on or after 1.4.1997 but before April 1, 2017 100% deduction from profits shall be allowed for 7 years from that year in which business of refining oil is started, provided undertaking is engaged in the business refining the mineral oil on or after 1.10.1998 but not after 31.03.2012. It begins commercial production of natural gas on or after 1.4.2009.

III. **In case of housing projects [Section 80 IB (10)]:** This deduction is allowed in connection with such projects which have been approved by local authority prior to 31.03.2008. This deduction is allowed in connection with those plots of land of which area is minimum one acre. .

If the residential unit is established within 25 kilo meter limit of Municipal Corporation of Delhi or Mumbai or within the cities of Delhi & Mumbai its built area should not exceed 1,000 square feet. If the residential unit is established at places other than Delhi and Mumbai, its built area should not exceed 1,500 square feet. 100% deduction from profits shall be allowed to those enterprises where the construction and development work starts on or after 01.10.1998 and construction completes on or before March 31, 2008 (where housing project is approved by local authority before April 1, 2004) or where housing project is approved during 2004-05, it should be completed within 4 year of the end approval year by of the financial year of the local authority or where housing project has been approved on or after April 1, 2005, the project should be completed within 5 years from the end of the financial year in which the housing project is approved by the local authority. For commercial establishment ceiling is of 3% of aggregate built of area or 5000 sq. feet, wherever is less.

- IV. **In case of hospitals in rural areas:** 100% deduction from profits shall be allowed for 5 assessment years starting from initial year in which undertaking begins to provide medical services subject of the fulfillment of following conditions:
- i) The hospital has the capacity of 100 beds facility for the patients.
 - ii) Hospital is constructed between 1.10.2004 to 31.03.2008 in accordance with the rules applicable and enforced by the local authority.
 - iii) The hospital has started functioning between 1.4.2008 and 31.03.2013.
- V. In case of storing and transportation of food grains: This deduction shall be allowed to those undertakings which are engaged in storing and transportation of food grains in the form of integrated business on or after 1.4.2001. 100% deduction to the company assessee will be allowed for first 5 years and 30% for next 5 years. Other assesses shall be allowed 100% deduction for first 5 years and 25% for next 5 years. The business of processing, preservation and packaging of meat and meat products or poultry or marine or daily products should commence on or after 31.03.2009.

9.5.17 Deduction in Respect of Profits from Housing Projects (Section 80- IBA)(With Effect from AY 2018-2019) :

This deduction is available to the assessee (may be individual, HUF, AOP, BOI, Company, firm or any other person) :

Conditions for deduction

- i) The housing project predominantly consists of residential units having facilities and amenities as the competent authority may specify.
- ii) The competent authority has approved the project after June 1, 2016 but upto March 31, 2019.
- iii) The project should be completed within a period of 5 years from the date of first approval of such project by the competent authority.
- iv) The project shall be considered and deemed to have been completed when a completion certificate of project (as a whole) is issued in writing by the competent authority and obtained by the assessee.
- v) Housing project cannot exceed 3% of the aggregate built up area for the use of carpet area of the shops and other commercial establishments.
- vi) Plot size, area of residential units, and minimum utilization of Floor Area Ratio (FAR) should satisfy following criteria :

Location of Project		
	Within the cities of Chennai, Delhi, Calcutta or Mumbai or within 25 km. from municipal limits	Any other Area
Plot area of the project	Not less than 1000 Sq. meters.	Not less than 2000 Sq. meters.
Area of residential units	Not to exceed 30 Sq. meters.	Not to exceed 60 Sq. meters.
Utilization of permissible FAR	Not less than 90%	Not less than 80%

- vii) Only one residential unit can be allotted to an individual in the housing project. No other residential unit can be allotted to that individual or his spouse or his minor children, to whom such one residential unit is allotted.
- viii) The assessee should keep and maintain separate books of accounts in respect of the housing project. c) Quantum of Deduction Subject to the fulfillment of the above conditions, 100% deduction of profits and gains derived from the business of developing and building a housing project.

Quantum of Deduction :

Subject to the fulfillment of the above conditions, 100% deduction of profits and gains derived from the business of developing and building a housing project.

9.5.18 Deduction in Respect of Profits and Gains from Undertaking in Special Category States (Section 80 IC) (w.e.f. A.Y. 2004-05) :

This deduction is allowed to all those assesses who are engaged in manufacturing any articles under the scheme of Central board of Direct Taxation (CBDT) in Export Processing Zone or Industrial park, Software Technology park, or Industrial area as notified by CBDT. Commodities specified in XIII Schedule shall not be included but articles specified in XIV Schedule shall be eligible for deduction.

Conditions for Deduction :

- i) Undertaking should not be formed by transferring old used plant and machine.
- ii) Undertaking should not be formed by splitting up or reconstruction of any old undertaking.

Quantum of Deduction :

100% deduction from profits shall be allowed for first 10 years if industrial undertaking is set up in Sikkim and production or expansion takes place between December

23, 2002 to March 31, 2007. Similarly, if the industrial undertaking is set up in Himachal Pradesh and Uttarakhand and product expansion takes place between Jan 07, 2003 to March 31, 2012, 100% deduction from profit should be allowed for first 5 year and 25% of profit (In case of a company 30%) for the industrial undertaking is set up in North Eastern states and starts production expansion between December 24, 1997 and March 31, 2007 the deduction shall be allowed as 100% of profit for first 10 years.

9.5.19 Deduction in Respect of Eligible Start up (Section 80 IAC) :

This deduction is allowed to start-up assessee who derives profits from Eligible Business.

Conditions for Deduction :

Eligible Start-Up Company or Limited Liability Partnership (LLP) engaged in eligible business subject to fulfilling following conditions can claim this deduction:

- i) It is incorporated on or after 01.04.2016 but before 01.04.2023.
- ii) Annual turnover of such company or LLP does not exceed Rs. 25 crores (Rs. 100 crore from the assessment year 2021-22) in the previous year relevant to the assessment year for which deduction is claimed u/s 80- IAC (1).
- iii) Such eligible start-up (company and LLP) holds a certificate of eligibility from the authority (Inter-Ministerial Board of Certification) as notified by Central Government.

Quantum of Deduction :

The assessee shall be allowed 100% deduction of profits and gains of such business for 3 consecutive years out of five years, (7 years for the assessment years 2018-19 to 2020-21),(10 years from the assessment year 2021-22)beginning from the year in which the eligible start-up is incorporated. Eligible Business means a business carried out by an eligible start-up engaged in innovation, development or improvement of products or processes or services or a scalable business model with high potential of employment generation or wealth creation.

9.5.20 Deduction in Respect of Profits and Gains from Business of Hotels and Convention Centers in Specified Area (Section 80 ID) :

This deduction is allowed to an assessee whose gross total income includes the profit and gain derived from business of a hotel located in National Capital Territory of Delhi.

Conditions for Deduction :

Deduction under this Section is subject to the fulfillment of the following conditions :

- i) An existing business should not be spitted or reconstructed to avail this deduction.
- ii) No existing building previously used as hotel or convention Centre (as the case may be) should be transferred to form such new eligible business.

- iii) Machinery or plant previously used for any purpose should not be transferred to form such new eligible business.
- iv) Return of Income is submitted before the due date u/s 139 (i).
- v) Audit report should be submitted along-with the return of income.
- vi) The benefit of deduction under this Section is allowed to the business of hotel (2, 3, 4 stars) in the specified area provided that it is constructed and has started working during the period between April 1, 2007 to July 31, 2010.
- vii) This deduction is also applicable to the business of hotels (2, 3, 4 star) situated in the specified districts having a world heritage site provided that it has started working during the period between April 1, 2008 to March 31, 2013.
- viii) If the business of building, owning and operating a convention Centre in specified area is carried out and such convention Centre is constructed during the period between April 1, 2007 to July 31, 2010.

Quantum of Deduction :

The assessee shall be allowed 100% deduction of profits earned from above mentioned businesses for 5 consecutive assessment years beginning from the initial assessment year.

9.5.21 Deduction in Respect of Certain Undertakings Carrying Business in North-Eastern States (Section 80-IE) :

This deduction is allowed to an assessee whose gross total income includes any profits and gains derived from certain undertakings established in North-Eastern States. It covers eligible services like hotels, business training institute, nursing home, hardware units, training center relating to IT.

Conditions for Deduction :

- i) If any undertaking is formed without splitting up or reconstruction of any existing business and without using more than 20% old plant and machinery (or total value of machinery in new business), in any of the North-Eastern States.
- ii) The assessee commences its operation of manufacturing or producing or substantial expansion to manufacture or produce or carry on any eligible business between the period 1st April, 2007 and March 31, 2017.
- iii) This deduction is allowed subject to the condition of furnishing Income-Tax Return u/s 139 (1) along-with audit report.

Quantum of Deduction :

The assessee shall be eligible for 100% deductions of profits and gains of such eligible business for 10 consecutive assessment years commencing from the previous year of manufacture or production or substantial expansion.

9.5.22 Deduction in Respect of Profits and gains from Business for Collecting and Processing of bio-Degradable waste (Section 80 JJA) :

This deduction is allowed for the above type of business only and is not allowed if such activity is carried out by job work customers.

Conditions for Deduction :

This deduction is disallowed if not claimed in the return of income.

Quantum of Deduction :

An assessee is allowed a 100% of deduction (for a period of 5 consecutive assessment years commencing from the previous year of commencement of business) from such gross total income that includes any profit and gains of the business of collecting and processing or treating of bio-degradable waste for generating power or producing biofertilizers, bio-pesticides or other biological agents or for producing biogas, making pallets or briquettes for fuel or organic manure.

9.5.23 Deduction in respect of employment of new employees[Section 80JJAA] :

A. Quantum of deduction available under this section :

A deduction of an amount equal to 30% of additional employee cost incurred in the course of such business in the previous year is allowed for 3 assessment years including the assessment year relevant to the previous year in which the employment is provided.

B. Conditions need to be fulfilled :

- 1) The business should be formed by splitting up or reconstruction of an existing business.
- 2) The business is not acquired by the assessee by way of transfer or as a result of any reorganisation of business.
- 3) Along with return of income, the repost of accountants to be provided.

C. Meaning of certain terms :

- **Additional employee cost :** Total remunerations paid or payable to additional employees employed during the previous year.

In case of an existing business - Nil,
if

- ✓ There is no increase in the number of employees than the total number of employees employed on the last day of the preceding year.
- ✓ remunerations are paid by an account payee cheque account payee bank draft or through of electronic clearing system by a bank account

In the first year of a new business

The remunerations paid or payable to employees employed during the previous year shall be considered as the additional employee cost.

- **Additional employee :** An employee who has been employed during the previous year and whose employment has resulted increase in the total number of employees employed by the employer on the last day of the preceding year except,
 - ✓ An employee whose total remunerations are more than Rs. 25,000 per month; or
 - ✓ An employee for whom the entire contribution is paid by the Government under the Employees' Pension Scheme.
 - ✓ An employee who is employed for a period of less than 240 days in the previous year and an employee employed for a period of less than 150 days during the previous year, in case of an assessee engaged in the business of manufacturing of apparel; or
 - ✓ An employee who has no contribution toward RPF in the recognised
 - ✓ provident fund.
- **Emoluments/Remunerations:** Any sum paid or payable to an employee in lieu of his employment, excluding
 - ✓ For the benefit of the employee, any contribution paid or payable by the employer to any pension fund or provident fund or any other fund under any law; and
 - ✓ lump-sum payments such as gratuity, leave encashment, voluntary retrenchment benefits, commutation of pension etc. paid or payable to an employee at the time of termination of his service/superannuation/voluntary retirement.

9.5.24 Deduction in Respect of Certain Income of Offshore Banking Units and International Financial Service Centre (Section 80 LA) :

If an assessee is a Scheduled Bank or a Foreign Bank, having unit of offshore banking in Special Economic Zone (SEZ) or a unit of International Financial Services and the Gross Total Income of such assessee includes :

- (i) Any income from the off shore banking unit in SEZ
- (ii) Any income from a business with an undertaking located in SEZ or any other undertaking which develops, operates and maintains a SEZ.
- (iii) Any income from any unit of the international financial services centre from its business for which it has been approved for setting up such a centre in a SEZ.

Conditions for Deduction :

- i) Deduction under this Section is available only when it is claimed in the return of income.
- ii) The above income should be earned in Convertible Foreign Currency.
- iii) The assessee shall have to submit a certificate of a chartered accountant in a prescribed form with return of income certifying that the deduction has been claimed correctly.

Quantum of Deduction :

A 100% deduction of the aforesaid income is allowed for 5 consecutive assessment years beginning with the assessment year relevant to the previous year in which permission for aforesaid business was obtained and thereafter 50% of such income for 5 consecutive assessment years.

Note :

- 1) Offshore banking means a branch of a bank located in a Special Economic Zone and which has obtained the permission under clause (a) of sub-Section (1) of Section 23 of Banking Regulation Act, 1949.
- 2) An international financial service means International Financial Service Center which has been approved by Central Government under subSection (1) of Section 18 of Special Economic Zone, 2005.

9.5.25 Deduction in Respect of Co-operative Societies (Section 80-P) :

- (a) Under this Section, 100% deduction shall be allowed for certain specified income of a co-operative society, engaged in specified activities subject to the condition that such income of the Society is included in the Gross Total Income of the Society.
- (b) 100% deduction is available from the profits and gains of Co-operative Societies carrying business of banking, cottage industry, marketing of agricultural produce (grown by members), purchase of articles (seeds, livestock etc.) for members, processing of members agriculture produce providing collective disposal of the labour of its member, fishing and allied activities, and primary societies business of supply of milk, fruits/vegetable and oilseeds.
- (c) In case of Consumer Co-operative Society, a deduction of upto Rs. 1,00,000 is allowed, while in any other case it is Rs. 50,000.

9.5.26 Deduction in respect of royalty income, etc., of authors of certain books other than textbooks [Section 80QQB] :

- Under this section a deduction up to Rs. 3 lakh is allowed to individuals resident in India for income derived being an author. The deduction shall be the income derived as author or Rs. 3 lakh whichever is less. This income can be a lump-sum of money or interest in the copy right of the book.
- However, this deduction will not be available for royalty income from school textbooks, guides, commentaries, newspapers, journals, pamphlets and other publications of same kind.
- For calculating the deduction under this section, the amount of eligible income, before allowing expenses attributable to such income, should not exceed 15% of the value of the books sold during the previous year. However,

this condition is not applicable where the royalty or copyright fees is receivable in lump sum for all rights of the author in the book.

9.5.27 Deduction in Respect of Royalty Income of Authors of Certain Books other than Textbooks (Section 80 QQB) :

This deduction is allowed to resident authors and co-authors who have been paid royalty in respect of copyright of books.

Conditions for deduction :

- (i) The manuscript of the book should be of work of literary, artistic or scientific nature.
- (ii) The term 'Book' shall not include guides, magazines, newspaper, journals or textbooks for school.
- (iii) If royalty is not paid in lump-sum and if it is based on percentage and the rate of royalty is more than 15% of the value of books during the year, deduction from Gross total income shall be allowed @ 15%.
- (iv) Deduction is not available unless it is claimed in the return of income.
- (v) No such deduction is allowed unless the assessee furnishes a certificate in the prescribed form (Form No. 10CCD), from the prescribed authority, along with return of income.
- (vi) When any royalty income is earned from outside India, then, so much amount of income shall be taken into account for the purpose of this Section as is brought into India by or on behalf of the assessee in convertible foreign exchange, within a period of six months from the end of the previous year in which such income is earned or within such further period as the competent authority may allow in this behalf. No deduction is allowed unless the assessee furnishes a certificate in the prescribed form (Form No. 10H), along with the return of income.

Quantum of Deduction :

A deduction of 100% of such royalty income or Rs. 3, 00,000, whichever is less, shall be allowed under this Section.

9.5.28 Deduction in Respect of Royalty on Patents (Section 80 RRB) :

This deduction is allowed to that individual who is resident in India and is a patentee.

Conditions for deduction :

- (i) The patent should be registered on or after 1st April, 2003 under the Patents Act, 1970.
- (ii) The assessee must have brought such income (Convertible foreign exchange) in India within 6 months from the expiry of the previous year.

- (iii) When any royalty income is earned from outside India, then, so much amount of income shall be taken into account for the purpose of this Section as is brought into India by or on behalf of, the assessee in convertible foreign exchange, within a period of six months from the end of the previous year in which such income is earned or within such further period as the competent authority may allow in this behalf.

Quantum of deduction :

A deduction of 100% of such income or Rs. 3,00,000, whichever is less is allowed under this Section.

9.5.29 Deduction in respect of interest on deposits in Savings Accounts [Section 80TTA]:

Under this section interest on deposits in savings account paid by an individual or HUF out of income, shall avail a deduction up to Rs 10,000 while calculating the total income of the assessee.

The deduction shall be allowed in case the saving account is maintained with :

- A banking company under Banking Regulation Act, 1949;
- A co-operative society involved in carrying on the business of banking; or
- A post office.

However, if interest paid on such account is held by or on behalf of a firm, an AOP/BOI, then no such deduction would be allowed.

9.5.30 Deduction in respect of interest on deposits earned by Senior citizens [Section 80TTB] :

The Government of India in the budget of 2018-19 has chosen to introduce a good number of benefits for senior citizens. One such important amendments in Budget 2018 (for senior citizens) is the introduction of a new section – Section 80 TTB.

Section 80TTB is a provision whereby a taxpayer who is a resident senior citizen, aged 60 years and above at any time during a Financial Year (FY), can claim a specified amount as a deduction from his gross total income for that FY. This section is applicable w.e.f. 1April 2018.

- **Quantum of deductions available :** A deduction of lower than Rs 50,000 or an amount from a specified income is allowed from the gross total income. Specified income is any of the following income in aggregate :
 - Interest on **bank deposits** (savings or fixed);
 - Interest on **deposits** held in a co-operative society engaged in the business of banking, including a co-operative land mortgage bank or a co-operative land development bank; or

- Interest on **post office deposits**
- **Exceptions to Section 80TTB:** If the specified deposits are held by or on behalf of a partnership firm, an association of persons (AOP) or a body of individuals (BOI), Section 80TTB deduction is not available for the partner of such a firm or for any member of such an AOP or BOI, while computing their total income.
- **Section 80TTA Vs. 80TTB:** Section 80TTA provides deductions similar to Section 80TTB. However, it provides deductions of interest only on savings account held in a bank, co-operative bank or a post office, from the gross total income of the individual taxpayer or a Hindu Undivided Family upto Rs 10,000.

With the introduction of Section 80TTB exclusively for senior citizens, deductions under Section 80TTA is not available to senior citizens.

<i>Difference between Section 80TTA and Section 80TTB</i>		
Particulars	Section 80TTA	Section 80TTB
Applicability	Applicable to individuals and HUF except for senior citizens	Applicable to senior citizens
Specified income	Interest on savings account only	Interest on all kinds of deposits
Quantum of deduction	Upto Rs 10,000	Upto Rs 50,000

9.5.31 Deduction in case of a Person with Disability [Section 80U] :

- Section 80U provides the criteria for being disable under income tax rules in accordance with the rules laid down by Persons with Disability (Equal Opportunity, Protection of Rights and Full Participation) Act, 1995.
- This Section is applicable to resident individuals who is certified by medical authority to be a person with disability at any time during the previous year.
- A deduction of Rs. 75,000 for a person with disability and Rs. 1,25,000 for a person with severe disability i.e. having disability over 80%, is allowed.
- Benefit of this deduction also extends to person suffering from autism, cerebral palsy and multiple disorders.
- The assessee claiming this deduction shall furnish a copy of certificate issued by medical authority in the form and manner as prescribed by the appropriate authority along with the return of income for the assessment year for which the deduction is claimed.

- In case the person needs reassessment, the assessee have to obtain a fresh certificate from the appropriate medical authority, after the expiry of the original certificate to keepin force the claiming of deduction under this section.

Maximum Allowed Tax Deduction Limits Under Section 80

Section	Deduction	Description	Maximum Limit
80C	Expenses and investments	Tuition fees, home loan principal, ELSS, PPF, NSC, etc.	Rs. 1,50,000
80CCC	Annuity pension plan	Payment made towards annuity pension plan	Rs. 1,00,000
80CCD	Central Government pension scheme	Amount paid towards a pension scheme under Central Government	Rs. 1,50,000
80CCF	Infrastructure bonds	Investments in Infrastructure bonds	Rs. 20,000
80D	Health insurance premiums	Premiums paid for health insurance policies	Rs. 1,00,000
80DD	Disabled dependent care	Expenses incurred for taking care of disabled dependent relative	Rs. 1,25,000
80DDB	Specific diseases expenses	Expenses made for specific diseases	Rs. 1,00,000
80E	Education loan payment	Payment towards education loan	No maximum limit
80EE	Home loan interest	Interest payments of home loan	Rs. 50,000
80EEA	Home loan (Apr 2019 – Mar 2020)	Home loan taken between April 1, 2019, and March 31, 2020	Rs. 50,000
80EEB	Electric vehicle purchase	Purchase of electric vehicles between April 1, 2019, and March 31, 2032, with a loan	Rs. 1,50,000
80G	Charitable donations	Donations to charitable funds and institutions	50-100% of donated amount
80GG	House rent allowance	House rent allowance deduction	Rs. 5000 per month
80GGB	Company political donations	Contribution or donation made towards a political party by an Indian company	No maximum limit
80GGC	Individual	Contribution or donation made	10% of gross total income

	political donations	towards a political party by an individual	
80IA	Industrial development	Tax deductions for organizations engaged in development, maintenance, operation of industrial parks, infrastructure facilities, power plant reconstruction, telecommunication services, and distribution of natural gas	Profit generated for 10 consecutive years
80J	New industrial establishments	Tax deduction facilities for new industrial establishments, hotels, and cruises in certain cases	Rs. 1,50,000
80LA	Offshore banking transactions	Transactions made through offshore banking or International Financial Service Centres (IFSC)	Rs. 1,50,000
80P	Co-operative society activities	Tax deductions on income involved in specific activities of a co-operative society	Rs. 1,00,000
80QQB	Royalty from book sales	Tax deduction benefits from the royalty earned from the sale of books	Rs. 3,00,000
80RRB	Royalty payments	Tax deduction on royalty payments	Rs. 3,00,000
80TTA	Savings account interest	Interest earned from savings accounts	Rs. 10,000
80TTB	Senior citizens' interest income	Interest income from deposits for senior citizens	Rs. 50,000
80U	Taxpayers with disabilities	Deductions available for taxpayers with disabilities	Rs. 1,25,000

9.6 SUMMARY :

The scheme of computing taxable income under the Income Tax Act is to first compute income under each head. The aggregate of income under each head is known as 'Gross Total Income'. Out of gross total income, certain deductions u/s 80 are allowed which are not for expenses incidental to earning the income but are of the nature of incentives aimed at achieving certain socio-economic goals through the instrumentality of taxation or provisions to mitigate hardships to tax-payers who have necessarily to incur certain personal expenditure. Such deductions are laid down in Chapter VI-A. The income after such deductions is called 'Total Income' which forms the basis for income tax.

One important point to remember is that the total of all deductions under Chapter VI-A cannot exceed the Gross Total Income. In other words, these deductions cannot result in 'Total income' being a negative figure, i.e., loss.

9.7 KEY WORDS :**Deductions :**

Permissible amount under Chapter VI-A by which the gross total income is reduced to arrive at the total income liable to tax.

Gross Total Income :

Aggregate of income computed under each head of income.

Total Income :

Amount of income computed in the manner laid down in the Income Tax Act on which tax is charged.

9.8 SELF ASSESSMENT QUESTIONS :

1. What is Gross Total Income? How do you compute it?
2. What is the deduction available under section-80IB in respect of housing projects?
3. What are the various items of donations allowed 100% of exemption U/S-80G?
4. What are some common deductions available to individuals?
5. Who is eligible to claim deductions U/S-80C of the Income Tax Act?

9.9 SUGGESTED READINGS :

1. R. K. Jain, Nikhil Gupta, Manoj Kumar Agrawal, Sanjeev S. Thakur, '*Practical Problems in Income Tax*', Scorer Guru Publications, Agra, 2023.
2. Dr. H. C. Mehrotra, Dr. S. P. Goyal, '*Problems and Solutions in Income Tax - Assessment Year 2022-23*', Sahitya Bhawan Publications, Agra, 2022.
3. Dr. H.C. Mehrotra, Dr. S.P. Goyal, '*Corporate Tax Planning & Management A.Y 2020-21 & 2021-22*', Sahitya Bhawan Publications, Agra, 2020.

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Lesson – 10
COMPUTATION OF TOTAL INCOME

Objectives :

After studying this lesson, you should be able to

- compute the taxable income,
- tax liability of an assessee after allowing certain deductions.

Structure of the lesson:

- 10.1 Introduction
- 10.2 Steps involved in Computation of Total Income
- 10.3 Solved Illustration on Computation of Total Income
- 10.4 Summary
- 10.5 Key Words
- 10.6 Self Assessment Questions / Illustrations
- 10.7 Suggested Readings

10.1 INTRODUCTION :

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. Let us go step by step to understand the procedure of computation of total income for the purpose of levy of income-tax.

10.2 STEPS INVOLVED IN COMPUTATION OF TOTAL INCOME :

Step 1 – Determination of Residential Status :

The residential status of a person has to be determined to ascertain which income is to be included in computing the total income.

The residential statuses as per the Income-tax Act are shown below :

In the case of an individual, the duration for which he is present in India determines his residential status. Based on the time spent by him, he may be

- (a) resident and ordinarily resident,
- (b) resident but not ordinarily resident, or
- (c) non-resident.

The residential status of a person determines the taxability of the income.

For e.g., income earned outside India will not be taxable in the hands of a non-resident but will be taxable in case of a resident and ordinarily resident.

Step 2 – Classification of income under different heads :

The Act prescribes five heads of income. These are shown below :

- Heads of income
- Salaries income from profits and gains capital income
- House property of business or gains from other
- Profession sources

These heads of income exhaust all possible types of income that can accrue to or be received by the tax payer. Salary, pension earned is taxable under the head “Salaries”. Rental income is taxable under the head “Income from house property”. Income derived from carrying on any business or profession is taxable under the head “Profits and gains from business or profession”. Profit from sale of a capital asset (like land) is taxable under the head “Capital Gains”. The fifth head of income is the residuary head under which income taxable under the Act, but not falling under the first four heads, will be taxed. The tax payer has to classify the income earned under the relevant head of income.

Step 3 - Exclusion of income not chargeable to tax:

There are certain incomes which are wholly exempt from income-tax, e.g. agricultural income. These incomes have to be excluded and will not form part of Gross Total Income. Also, some incomes are partially exempt from income-tax e.g. House Rent Allowance, Education Allowance. These incomes are excluded only to the extent of the limits specified in the Act. The balance income over and above the prescribed exemption limits would enter computation of total income and have to be classified under the relevant head of income.

Step 4 - Computation of income under each head:

Income is to be computed in accordance with the provisions governing a particular head of income. Under each head of income, there is a charging section which defines the scope of income chargeable under that head. There are deductions and allowances prescribed under each head of income. For example, while calculating income from house property, municipal taxes and interest on loan are allowed as deduction. Similarly, deductions and allowances are prescribed under other heads of income. These deductions etc. have to be considered before arriving at the net income chargeable under each head.

Step 5 – Clubbing of income of spouse, minor child, etc. :

In case of individuals, income-tax is levied on a slab system on the total income. The tax system is progressive i.e. as the income increases, the applicable rate of tax increases. Some taxpayers in the higher income bracket have a tendency to divert some portion of their income to their spouse, minor child etc. to minimize their tax burden. In order to prevent such tax avoidance, clubbing provisions have been incorporated in the Act, under which income

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

Step 6 – Set-off or carry forward and set-off of losses :

An assessee may have different sources of income under the same head of income. He might have profit from one source and loss from the other. For instance, an assessee may have profit from his textile business and loss from his printing business. This loss can be set-off against the profits of textile business to arrive at the net income chargeable under the head “Profits and gains of business or profession”.

Similarly, an assessee can have loss under one head of income, say, Income from house property and profits under another head of income, say, Profits and gains of business or profession. There are provisions in the Income-tax Act for allowing inter-head adjustment in certain cases. Further, losses which cannot be set-off in the current year due to inadequacy of eligible profits can be carried forward for set-off in the subsequent years as per the provisions contained in the Act.

Step 7 – Computation of Gross Total Income :

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

Step 8 – Deductions from Gross Total Income :

There are deductions prescribed from Gross Total Income.

Step 9 – Total income :

The income arrived at, after claiming the above deductions from the Gross Total Income is known as the Total Income. It is also called the Taxable Income. It should be rounded off to the nearest Rs.10.

Step 10 – Application of the rates of tax on the total income :

The rates of tax for the different classes of assesses are prescribed by the Annual Finance Act.

Step 11 – Surcharge :

Surcharge is an additional tax payable over and above the income-tax. Surcharge is levied as a percentage of income-tax. At present, the rate of surcharge for firms and domestic companies is 10% and for foreign companies is 2.5%. For individuals, surcharge would be levied @10% only if their total income exceeds Rs.10 lakhs.

Step 12 – Education Cess :

The income-tax, as increased by the surcharge, is to be further increased by an additional surcharge called education cess@2%. The Education cess on income-tax is for the

purpose of providing universalised quality basic education. This is payable by all assesses who are liable to pay income-tax irrespective of their level of total income.

Step 13 - Advance tax and tax deducted at source :

Although the tax liability of an assessee is determined only at the end of the year, tax is required to be paid in advance in certain installments on the basis of estimated income. In certain cases, tax is required to be deducted at source from the income by the payer at the rates prescribed in the Act. Such deduction should be made either at the time of accrual or at the time of payment, as prescribed by the Act. For example, in the case of salary income, the obligation of the employer to deduct tax at source arises only at the time of payment of salary to the employees. Such tax deducted at source has to be remitted to the credit of the Central Government through any branch of the RBI, SBI or any authorized bank. If any tax is still due on the basis of return of income, after adjusting advance tax and tax deducted at source, the assessee has to pay such tax (called self-assessment tax) at the time of filing of the return

10.3. SOLVED ILLUSTRATIONS

Illustration – 1 : Compute the deduction allowed U/s-80C from the following information furnished by Mr. X for the assessment year 2023-24.

	Rs.
Gross total income	4,85,000
Contribution to Statutory provident fund	20,000
Insurance premium paid on his own life (Policy issued on 01.04.2015, Sum assured Rs. 20,000)	6,000
Insurance premium paid on the life of father	4,800
Insurance premium paid on the life of his wife	2,000
Life insurance premium paid on the life of his not dependent major son	2,500
Life insurance premium paid on the life of dependent brother	2,000
Insurance premium paid on the life of married daughter on a policy of Rs. 50,000, issued in 2011	12,000
Amount deposited in PPF	15,000
Contribution to Sukanya Samriddhi Account	50,000
Tuition fees paid for his 3 sons education (Rs. 2,500+Rs. 2,800+Rs. 3,400)	8,700
Purchase of NSC IX issue	20,000
Contribution towards LIC Mutual Fund	2,000
Term deposit for 5 years (Tax Saving) with S.B.I.	30,000
Five year time deposit in post office	10,000
Contribution to ULIP	5,000
Repayment of Housing Loan taken from S.B.I. (Interest Rs. 25,000 + Principal Amt. Rs. 20,000)	45,000

Solution:

Computation of Deduction Allowable U/s-80 C for assessment year 2023-24

	Rs.
Contribution to Statutory provident fund	20,000
Insurance premium paid on his own life	6,000
Insurance premium paid on the life of father (Not Allowed)	Nil
Insurance premium paid on the life of his wife (Spouse)	2,000
Life insurance premium paid on the life of his not dependent major son	2,500
Life insurance premium paid on the life of dependent brother (Not Allowed)	Nil
Insurance premium paid on the life of married daughter (Maximum 20% of sum assures)	10,000
Amount deposited in PPF	15,000
Contribution to Sukanya Samriddhi Account	50,000
Tuition fees paid for his 2 sons education (Rs. 2,800+Rs. 3,400)	6,200
Purchase of NSC IX issue	20,000
Contribution towards LIC Mutual Fund	2,000
Term deposit for 5 years (Tax Saving) with S.B.I.	30,000
Five year time deposit in post office	10,000
Contribution to ULIP	5,000
Repayment of Housing Loan taken from S.B.I. (Principal Amt. Rs. 20,000)	20,000
Gross Total	1,98,700

Qualifying amount for deduction U/s-80C restricted to Rs.1.50,000.

Hence, Taxable Income = Gross Total Income – Deductions U/S-80C,

$$\text{i.e., } 4,85,000 - 1,50,000 = \text{Rs.}3,35,000.$$

Illustration – 2 : Kamal, a resident of India furnishes the following information regarding his income in the previous year.

	Rs.
Gross Total Income (Profits from proprietary business Rs. 40,00,000, profit share of an AOP Rs. 10,00,000, Interest on securities (Gross) Rs. 10,00,000; ¼ share in a firm's profit Rs. 5,00,000)	60,00,000
Donations to:	
(i) National Defence Fund (NDF)	50,000
(ii) Jawahar Lal Nehru Memorial Fund (JLNMF)	75,000
(iii) For repairs and renewal of Gurudwara famous for worship in the state	1,00,000
(iv) Amount paid for renewal of a famous temple (not notified)	1,00,000

(v) National children fund (NCF)	20,0500
(vi) Prime Minister National Relief Fund (PMNRF)	30,000
(vii) Contribution in Swachh Bharat Kosh	50,000
(viii) Contribution for room construction in Woman Protection Home (Capital nature) (Notified)	20,000
(ix) Contribution in Andhra Pradesh Chief Minister Cyclone Relief Fund	50,000
(x) Contribution in Clean Ganga Fund	50,000
(xi) Contribution for Jain Dharamshala repairs	25,000
(xii) Contribution to Indira Gandhi Memorial Trust	50,000
(xiii) Contribution for promoting family planning (Govt. programme)	1,00,000
(xiv) Contribution to Nagar Mahapalika for public water taps	2,50,000
(xv) Contribution to charitable institution (approved u/s 80 G)	1,50,000
(xvi) Contribution for repair of world-famous historical building	50,000
(xvii) Contribution to National Trust for welfare of persons with Autism, cerebral palsy, mental retardation and multiple disabilities	50,000
(xviii) Contribution to Prime Minister's Drought Relief Fund (PMDRF)	1,50,000

He contributed Rs. 20,000 towards units of Mutual Fund (Notified) and paid Rs. 25,000 as Tuition Fee of his son who is medical student. He contributed Rs. 40,000 in P.P.F. Account of his wife and son. He invested Rs. 50,000 in listed equity shares under a notified saving scheme of the Government and Rs. 10,000 in listed units of an Equity oriented fund. Compute Taxable Income of Mr. Kamal for the Assessment Year 2023-24.

Solution :

Computation of Taxable Income of Mr. Kamal for Assessment Year 2023-24

			Rs.	Rs.
(a) Income from Business/Profession				
	(i)	Profit from Proprietary business	40,00,000	
	(ii)	Share in AOP	10,00,000	
	(iii)	¼ share in profit in a Firm	Exempt	50,00,000
(b) Income from other sources:				
	(i)	Interest on securities		10,00,000
Gross Total Income				60,00,000
Less: Deductions				
	(i)	U/s-80C for investments, etc (Rs.20,000 + 25,000 +40,000)	85,000	
	(ii)	U/s-80CCG for investment in Listed Equity Shares and Listed Units of an Equity Oriented Fund	Nil	

	(iii)	U/s-80G:		
		(a) For Donations 100% of Rs.4,00,000 (Aggregate of donations of I & III categories)	4,00,000	
		(b) % of Rs.6,66,500 (II & IV categories total, i.e., Rs.2,75,000 + 3,91,500)	3,33,250	8,18,250
Taxable Income				51,81,750

Working Notes :

I. Category Donations (100%)			II. Category Donations (50%)		
		Rs.			Rs.
(a)	NDF	50,000	(a)	JLNMF	75,000
(b)	PMNRF	30,000	(b)	PMDRF	1,50,000
(c)	NCF	20,000	(c)	Indira Gandhi Memorial Trust	50,000
(d)	Swatch Bharat Kosh	50,000			2,75,000
(e)	APCMCRF	50,000			
(f)	Clean Ganga Fund	50,000			
(g)	National Trust for Welfare of Autism, etc.	50,000			
		3,00,000			
III. Category Donations (100% of Q.D.)			IV. Category Donations (50% of Q.D.)		
		Rs.			Rs.
	Contribution for Family Planning	1,00,000	(a)	Approved Charitable Institutions	1,50,000
			(b)	Nagar Mahapalika Water Taps	2,50,000
			(c)	Repair of Historical Building	50,000
			(d)	Gurudwara Renewal	1,00,000
		1,00,000			5,50,000

Combined qualifying amount for donations of III & IV category will be the least of the following :

- i) Total donation under both categories (1,00,000 + 5,50,000) = 6,50,000
- ii) 10% of adjusted total income i.e. 10% of Rs. 49, 15,000.

[Rs. 60, 00,000 (GTI) – Rs. 85,000 (80 C) – Rs. 10, 00,000 (share in AOP) = Rs. 4,91,500. Hence Q.D. = Rs. 4,91,500 out of which Rs. 1,00,000 is for promoting family planning which will be deducted @ 100% and the balance of Rs. 3,91,500 [Rs. 4,91,500 – 1,00,000] will be deductible @ 50%.]

Illustration – 3 : Mr. Harish of Delhi furnishes the following information in respect of Assessment year 2023-24

	Rs.
(a) Gross total income	6,00,000
(b) Life Insurance Premium paid (Policy Amount Rs. 70,000; policy is issued before 01.04.2012)	17,500
(c) Donation in Swachh Bharat Kosh	10,000
(d) Health Insurance Premium paid on the health of his child (By cheque)	5,000
(e) Amount spent on the medical treatment of his disabled father who is fully dependent on him (A proper certificate of disability is obtained)	75,000
(f) Mr. Harish resides in a rented house in Delhi and pays Rs. 9,000 p.m. He does not own any residential house anywhere but has a factory at Aligarh, rent income of which is included under the head 'Income from other sources'	

Compute taxable income of Mr. Harish for AY 2023-24.

Solution :

Computation of Taxable Income of Mr. Harish for Assessment Year 2023-24

	Rs.	Rs.
Gross total income		6,00,000
Less: Deductions		
U/s-80C (20% of sum assured as the policy is issued before 01-04-2012)	14,000	
U/s 80-D for Health Insurance	5,000	
U/s 80-DD for medical treatment of disabled father	75,000	
U/s 80-G donation in Swachh Bharat Kosh (100%)	10,000	
U/s 80-GG for rent paid (See Note)	58,400	1,62,400
Taxable Income		4,37,600

Working Notes :

(1)	LIP restricted to 20% of sum assured as the policy is taken before 01.04.2012	
(2)	Least of the following is deductible U/s 80-GG:	Rs.
	(i) Rs. 5,000 p.m.	60,000
	(ii) 25% of adjusted total income [Rs. 4,96,000 × 25/100]	1,24,000
	(iii) Rent paid in excess of 10% of adjusted total income i.e. [Rs. 1,08,000 (12×9,000)-10% of Rs. 4,96,000]	58,400
	(iv) Adjusted total income = [Rs. 6,00,000 – Rs. 14,000 (80-C) – Rs. 5,000 (80-D) – Rs. 75,000 (80-DD) – Rs. 10,000 (80-G) = Rs. 4,96,000]	

Illustration – 4 : Mr. Ramoji commenced business on 1st April, 2014. He furnishes the following information for the previous year 2022-23.

		Rs.
(a)	Income from the business of collecting and processing of bio-degradable waste for producing bio fertilizer	2,60,000
(b)	Taxable Income from House Property	3,50,000
(c)	Income from poultry farming	92,000
(d)	Income from livestock Breeding	95,000
(e)	Dividend from units of UTI	5,000
(f)	Interest on Govt. Securities	8,000
(g)	Dividend on shares of foreign co.	5,000
(h)	Interest on saving bank account in a nationalized bank	62,000
(i)	Life insurance premium paid on a policy of Rs. 50,000 policy taken before 01.04.2012	14,000
(j)	Life insurance premium paid on a policy of Rs. 1,20,000 policy taken on 01.04.2017	15,000
(k)	Royalty income on a book authored by Mr. Ramoji (book is acknowledged as work of artistic nature)	3,20,000

Compute the Taxable Income of Mr. Ramoji in the following cases :

- a) When his age is 46 years.
- b) When his age is 65 years.
- c) Mr. Ramoji qualifies U/s 80 QQB.

Solution:

Computation of Taxable Income of Mr. Ramji for Assessment Year 2023-24

		Age – 46 Year (Case-A) Rs.	Age – 65 Year (Case-B) Rs.
(a)	Income From Housing property	3,50,000	3,50,000
(b)	Income from business or profession :		
	(i) Income from business of collecting and processing of Bio-degradable waste	2,60,000	2,60,000
	(ii) Income from poultry farming	92,000	92,000
	(iii) Income from livestock breeding	95,000	95,000
(c)	Income from other sources :		
	(i) Dividend from UTI	Exempt	Exempt
	(ii) Interest on Govt. Securities	8,000	8,000
	(iii) Dividend from foreign company	5,000	5,000
	(iv) Interest on saving bank interest	62,000	62,000
	(v) Royalty income	3,20,000	3,20,000
	Gross Total Income (GTI)	11,92,000	11,92,000

Less : Deductions

(i)	U/s 80 C	Rs.		
	(a) Int. on Govt. Securities	8,000		
	(b) 20% of 50,000 Policy	10,000		
	(c) 10% of 1,20,000 Policy	12,000		
		30,000		
(ii)	U/s JJA 100% profit	2,60,000		
(iii)	U/s QQB Royalty	3,00,000	5,90,000	5,90,000
		5,90,000	6,02,000	6,02,000
(iv)	U/s 80 TTA		10,000	---
(v)	U/s 80 TTB		--	50,000
Net Taxable Income			5,92,000	5,52,000

Illustration – 5 :

Y Ltd is in the construction business of residential and commercial properties in Mumbai. In April, 2016, it acquires a plot of land of 1800 square meter in a locality (which is situated at a distance of 18 km. from Mumbai). The company wants to construct residential units on the plot of land for which approval is taken from the local authority on June 10, 2016. Area of each residential unit will be 30 square meter. Y Ltd maintains separate books of accounts for this project. Income of Y Ltd from various sources (before deduction under chapter -VI A) is as under:

(Rs. in Lakh)

Previous Year	Income from Housing project in locality	Income from Other housing project	Total Income
2019-20	-70	970	900
2020-21	300	900	1200
2021-22	530	-30	500
2022-23	500	1100	1600

The Housing Project in locality is completed on April 20, 2021. Completion certificate is issued by local authority on May 1, 2021. Other required conditions u/s 80-IBA are satisfied. Compute the amount of deduction available u/s 80-IBA.

Solution :

Since all the conditions are met by the assessee, U/s 80-IBA, therefore, assessee is eligible for the following deduction u/s 80-IBA.

(Rs. in Lakh)

Previous Year	Assessment Year	Income from eligible Housing project	Deduction U/s- 80-IBA
2019-20	2020-21	-70	Nil
2020-21	2021-22	300	300
2021-22	2022-23	530	500 (Note)
2022-23	2023-24	500	500

10.4 SUMMARY :

The assessee pays tax on his total income. This total income is nothing but the aggregate of taxable income from each head i.e., salaries, house property, business and profession, capital gains and income from other sources. From this aggregate income, the carried forward losses are set off and the permissible deductions under Chapter-VIA are allowed. The resulting figure is the taxable income of the assessee. Income tax is charged on the taxable income according to the tax rate specified by the Finance Act for that assessment year.

10.5 KEY WORDS :**Deductions :**

Permissible amount under Chapter VI-A by which the gross total income is reduced to arrive at the total income liable to tax.

Gross Total Income :

Aggregate of income computed under each head of income.

Total Income :

Amount of income computed in the manner laid down in the Income Tax Act on which tax is charged.

Surcharge :

It is additional tax levied by Central Government to generate revenue for specific purpose. It is charge at a specific rate on the amount of tax on taxable incomes.

Health & Education Cess :

It is an additional tax imposed and collected by Central Government for meeting funds required for health and education of the country.

10.6 SELF ASSESSMENT ILLUSTRATIONS ON COMPUTATION OF TOTAL INCOME :

Illustration – 1 : Mr. Ram who is a person with disability submits the following information. Compute (a) the Taxable Income (b) the Tax payable for the assessment year 2023-24

		Rs.
(i)	Salary (per annum)	3,00,000
(ii)	Rent received	48,000
(iii)	Dividend from Co-operative Society	1,000
(iv)	Interest on Savings Bank Deposits	18,000
(v)	Interest on government securities	1,000
(vi)	Winning from Lotteries (gross)	5,000
(vii)	Dividend on shares of foreign co.	10,000
(viii)	Deposit under PPF Scheme	30,000

Illustration – 2 : Rahul who is a resident in India, is a person with disability, he provides the following particulars of his income for the year ended 31.3.2023.

		Rs.
(a)	Salary for working as a Cable Operator (per month)	18,000
(b)	Interest on Government Securities (gross)	45,000
(c)	Honorarium from school of orphanage for giving his service	49,000

He has donated Rs. 20,000 to the school for orphanage which is approved as a charitable institution and contributed Rs. 2,000 to prime Minister national Relief Fund, he has also paid Rs.3,000 by credit card as premium of mediclaim policy, his father is also a person with disability and is dependent on him for medical treatment and rehabilitation. Rahul spends Rs. 8,000 during the year on him. Compute the Total Income for the Assessment Year 2023-24, assuming he has deposited Rs. 20,000 in public provident fund Account.

Illustration – 3 : Following are the particulars of income of Mr. Ram, who is 70 years old resident in India, for the Assessment year 2023- 24: Gross Total Income Rs. 8,10,040 which includes long-term capital gain of Rs. 2,55,000, Short-term capital gain of Rs. 88,000, interest income of Rs. 12,000 from savings bank deposits with banks. Mr. Ram invested in PPF Rs. 1,40,000 and also paid a medical insurance premium Rs. 31,000. Compute the total income of Mr. Ram.

Illustration – 4 : From the following information compute the total income of an individual for the Assessment year 2023-24 :

- (a) Salary after deduction of provident fund contribution and income tax Rs.3,27,000.
- (b) Income tax deducted on salary Rs.3,000.
- (c) His contribution to recognized provident fund Rs.20,000.
- (d) Employer's contribution to provident fund Rs.20,000.
- (e) Interest credited to provident fund Rs.6,200 @ 9.5%.

- (f) Net dividends received from domestic company Rs.8,950.
- (g) Interest on Savings Bank A/c Rs.3,000.
- (h) Life insurance premium paid Rs.2,000.

Illustration - 5:

Mr. X provides the following particulars of his income for the previous year ended on 31st March 2023 :

- (a) Basic salary Rs.40,000 p.m.
- (b) Bonus Rs.50,000
- (c) He owns a house property and the same is let out for a monthly rent of Rs.10,000
- (d) Municipal value of the house is Rs.96,000.
- (e) Municipal taxes paid by him amounted to Rs.12,000 p.a.
- (f) He received interest on unlisted debentures 9,000 and interest on fixed deposits in a bank Rs.4,400.
- (g) He paid life insurance premium of Rs.20,000 on a policy taken in 2014 (sum assured being Rs.2,50,000).

He also paid the following donations :

- (i) Bangalore Municipal Corporation for promotion of family planning Rs.65,000 by cheque.
- (ii) The Prime Minister's Drought Relief Fund Rs.7,000
- (iii) The Prime Minister's National Relief Fund Rs.10,000.

You are required to compute the taxable income of Mr. X for the Assessment Year 2023-24.

10.7 SUGGESTED READINGS :

1. R. K. Jain, Nikhil Gupta, Manoj Kumar Agrawal, Sanjeev S. Thakur, '*Practical Problems in Income Tax*', Scorer Guru Publications, Agra, 2023.
2. Dr. H. C. Mehrotra, Dr. S. P. Goyal, '*Problems and Solutions in Income Tax - Assessment Year 2022-23*', Sahitya Bhawan Publications, Agra, 2022.
3. Dr. H.C. Mehrotra, Dr. S.P. Goyal, '*Corporate Tax Planning & Management A.Y 2020-21 & 2021-22*', Sahitya Bhawan Publications, Agra, 2020.
4. J.C. Varshney & Nikhil Gupta, "Corporate Tax Planning", SBPD Publication, Agra, 2022.

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