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INCOME - TAX

1. INTRODUCTION

Meaning of Income-Tax : Broadly speaking, the Income-Tax means “the tax payable by a person, an individual, an organisation on over and above the income earned during a particular year, as per the Income-Tax Rules which come into force from time to time in the said particular year”.

It is quite clear that, the income differs from person to person, and, an organisation to an organisation. If the Income-Tax is not being levied by the Government on the basis of incomes of persons or organizations, the rich become richer and the richer becomes richest. And in turn, the poor becomes poorer and the poorer becomes poorest.

One of the main source of the income to the Government is through levying tax on income.

But, the Government has to keep the following points in view before levying the tax on income.

1. Financial position of the common people.
2. Tax bearing capacity of the public.
3. Appraisal of the various welfare activities and programmes of the Government.
4. Financial position of the country.

During the olden days the government’s main aim was to maintain peace and harmony in the country and to protect the public by all means. But, now- a-days the Government’s aim has become very broad. And its functions have become multi-dimensional. The trend has developed towards the various public welfare measures and programmes besides other functions. For which huge amounts are to be required to the Government. So, the levying of tax has become a must to the Government.

The taxes are of two kinds.

TAXES

Direct Taxes | Indirect Taxes

Let us know about these taxes one after the other.

1. Direct Taxes : “Direct Taxes are those taxes which are being collected by the Government, directly from the person concerned”.

   Examples :
   1. Income Tax
   2. Wealth Tax
   3. Gift Tax etc.

2. Indirect Taxes : “Indirect Taxes are those taxes which are not levied directly but levied indirectly”.

Examples :
1. Sales Tax
2. Entry Tax
3. Excise Duty
4. Customs Duty etc.

In order to understand clearly, let us see the following diagram.

TAXES

Direct Taxes	(Example of Direct Tax)	Indirect Taxes	Example of Indirect Tax
The Tax payer ↓ Directly pays the Tax to ↓ The Government	The income earned Person ↓ Directly pays the tax to ↓ The Government (Income-Tax)	The Tax Payer ↓ Middlemen ↓ The Taxpayer Pays the tax to to the middlemen and the middlemen in turn deposit to ↓ The Government	Consumer ↓ Trader ↓ (The consumer while purchasing an article will pay the tax to the trader i.e., cost of the article includes tax and in turn the trader deposit to ↓ The Government Sales Tax

The Main purpose of the Income tax law is that,
1. To reduce the inequalities in Income and Wealth by taxing the rich at the higher rates.
2. To raise the income to the Government to provide various welfare measures to the Public/Society at large.

The Income -Tax was introduced in India, in the year 1860 by Sir James Wilson, the British Rulers at first of its kind, following the mutiy of 1857. The Act provides for the General Tax on Income and also laid down the certain procedure in levying the tax. This pattern is the process till to-day with slight changes from time to time. And this Act has excluded the Agricultural income from its scope.

The Income-Tax Act was passed in the year 1918 and 1922. The former remained in its operation for four years and the later is in its operation till to the new Income-Tax Bill which come into force in the year 1961.

The Bill which was passed in September 1961, and came into force from Ist April 1962 in the whole of the country including the state of Jammu and Kashmir and the Union Territories, on the recommendations of,

I. Law commission and

II. Direct taxes enquiry Committee

in consultation with the Law Ministry.

The Income-Tax Act, 1961 is very comprehensive, consisting of 298 sections, running into thousand' sub –sections, Schedules, Rules, Sub-Rules etc., supported by other Acts and Rules.

It has been ammended in the year 1975 and 1984 with the aim at devising measures for unearthing black money and preventing its proliferation, combating tax evasion: checking avoidance of tax through illegal devices including formation of trusts and diversion of income or wealth to members of family, reducing the tax arrears, rationalizing the exemptions and deductions available under the Income Tax Act of 1961. And also several amendments were made from time to time with the aim of enlarging the scope of taxation.

The main hierarchy in implementing the Income Tax Act is as follows :

Finance Ministry

Central Board of Direct Taxes

Income-Tax Department

The Finance Ministry is at apex level, which prepares the Budget alongwith Finance Bill and submits the same before the parliament every year by the finance Minister on the last day of February. The Finance Bill discloses the Financial policy of the Government. After taking the assent from the both the Houses the Finance Bill is bering sent to the President for his consent. After getting the consent, by the President the Bill will become an Act. And the Act will come into execution. The Finance Act, reveals the ceiling of the income, the tax rates and exemptions thereon.

The Central Board of Direct Taxes, which frames the rules and regulations for execution of the Act and issues the circulars on the doubts raised by the Income Tax Department and by the public. Thus, it helps to the Income-Tax Department and to the public.

The Income-Tax Department deals with the tax execution.

The detailed hierarchy is being discussed in the coming chapters.

If the circulars being issued by the Income-Tax Authorities are not satisfied by the tax payer in such cases the tax payer is having the full liberty to approach the the High Courts of the states and Supreme Court for justification.

In order to know the income-tax rules and regulations, thoroughly, one should have to know the basic concepts involved in it. So, let us discuss about the Basic concepts one after the other in the coming units.

SUMMARY

- The word Income-Tax is the combination of two words
  i) Income and ii) Tax on such income.
- Income-Tax means, "the Tax payable by a person, an individual, an organisation, on over and above the income earned during a particular year, as per the Income-tax rules which come into force from time to time in the said particular year".
- If the Income-Tax is not being levied by the Government in such case, the rich becomes richer and the richer becomes richest, and inturn the poor becomes poorer and the poorer becomes poorest.
- One of the main source of income to the Government is through levying tax on income.
- Taxes are of two kinds, I) Direct Taxes, ii) Indirect Taxes.
- Direct Taxes are those taxes which are being imposed by the Government to reduce and minimise the financial imbalances balances and differences.
- Indirect taxes are those taxes which are not levied directly on income but levied indirectly.
- Income-Tax falls under the Direct Taxes.
- The Income-Tax was introduced in India in the year 1860 by the British Rulers, following the mutiny of 1857.
- The Income Tax Act, 1961, which come into force from 1st April, 1962, in the whole of the country, consisting of 298 sections, thousands sub-sections, Schedules, Rules, Sub-Rules etc.

QUESTIONS

Short Questions:

1. What is meant by income-tax ?
2. How many types of taxes are there ? What are they?
3. What is meant by Direct Taxes ?
4. Give any two examples of Direct Taxes ?
5. What is meant by Indirect Taxes ?
6. Give any two examples of Indirect Taxes ?
7. Explain in brief the introduction of income tax in India ?
8. Every year on which day the Finance Minister submits the Finance Bill before the Parliament ?
9. What is the main duty of the Central Board of Direct Taxes ?

ESSAY TYPE QUESTION :

1. Explain the brief History of Income Tax in India ?

2. BASIC CONCEPTS

The various concepts have been defined under section2, of the Income Tax Act, 1961, they are :

ASSESSEE [Under Section 2(7)]

The concept of “Assessee” has been defined under section 2, sub-section 7 of the Income-Tax Act, 1961, is as follows :

“Assessee” means a person by whom any tax or any other sum of money is payable under this Act, and includes :-

a) Every person in respect of whom any proceedings under this Act have been taken for the Assessment of his income or of the income of any other person in respect of which he is assessable or the loss sustained by him or by such other person or of the amount of refund due to him or to such other person.
b) Every person who is deemed to be an assessee under any provision of this Act.
c) Every person who is deemed to be an assessee in default under any provision of this Act.

If we elaborate the above definition, the following points can be emerged.

1) Every person by whom any tax or any other sum of money is payable under this Act.

Example: Mr.Raghu Ram Kothwal’s total income from all the sources come to Rs.1,00,000/- during the year 2003-2004. So, the incumbent has to pay the tax as per the Income Tax Act. Hence, Mr.Raghu Ram Kothwal will become an Assessee.

2) Every person inrespect of whom any proceedings under this Act have been taken for the assessment of his income.

Example: The Assessing Officer has issued a notice under the Income Tax Act in respect of Sri.Dr.Jai Prakash of Banswada, Nizamabad District on his earnings for the assessment of the income. Hence, Dr. Jai Prakash will be an Assessee, if his profession turnover seems to be exceeded Rs.10,00,000/- per year.

3) For the Assessment of his own income.

Example: Mr.P.Gopal Rao has earned an income of Rs.1,00,000/- during the year 2004-2005. For which he has to file the income-tax returns for asessment. Hence, Sri. P.Gopal Rao will become an Assessee.

4) Of the income of any other person inrespect of which he is assessable.

Example: Sri. Ch. Krishna Murali is the Guardian of Mr.A. Venkat Ram Reddy a minor. Mr.A. Venkat Ram Reddy has earned an income of Rs.1,00,000/- during the year 2004-2005 of the income of Mr.A.Venkat Ram Reddy, if Sri. Ch.Krishna Murali is being assessed, in such case, Sri. Ch. Krishna Murali will be treated as deemed Assessee to pay the tax on the income of the minor Mr.A.Venkat Ram Reddy.

5) Of the loss sustained by him or by such other person.

Example: Sri.B.Shanker has organised a Shiva Chits & Finance Ltd., and put into loss by Rs.1,00,000/- of the loss Sri.Dr.J.Gangadhar and Sri. Nagulagam Vittal have sustained. Hence, Sri. B.Shanker, Dr. J. Gangadhar and Sri.N.Vital will be treated as "Assessees".

6) Of the amount of refund due to him or to such other person.

Example: Sri.Siddamsetti Satyanarayana, proprietor of M/s. Veerabhadra Dresses has paid excess income-tax over his earnings. For which the income tax authorities have to refund the same. Hence, Sri. S.Satyanarayana will become an Assessee.

7) Every person who is deemed to be an assessee under any provision of this Act : Legal representatives of a deceased Assessee is to be called as deemed to be an Assessee under the income Tax Act.

Example: Sri. Shivarajaiah is a legal representative of Mr.Narla Rajashekar. And Mr. Narla Rajashekar, a minor has earned an income of Rs.1,00,000/-. But, he has not filed the income-tax returns. Hence, Sri. Shivarajaiah is deemed to be an assessee from the income-tax point of view.

8) Every person who is deemed to be an Assesseee in default under any provisions of this Act.

Example: 1.Sri. M.Shiva Ram Kothwal has to deduct the tax at source in accordance with the provisions of he income tax Act. But he fails to do so.
2. Sri.K.Bhasker, an employe of M/s. Surya Tubes Ltd., has become a defaulter under the income-tax Act in submitting his income tax returns as the employer fails to deduct the tax and to deposit the said amount to the Government.
In such cases Sri. M.Shivaram Kothwal and Sri.K.Bhasker both of them will become an Assessees indefault under this act.

Thus, Assessee is a person who has to file his income tax returns as per the Income tax Act, and to pay the tax thereon, if any.

PERSON [Under Section 2(3)]

As per the Income Tax Act, 1961, under Section (2) and sub-section (3), the "person" includes :-

1) An individual
2) An association of persons or a body of individuals whether incorporated or not
3) A Hindu undivided family
4) A firm
5) A company
6) A local authority
7) Every artificial judicial (legal) person, not falling within any of the preceding sub-clauses.
8) A statutory corporation
9) A state government which carries or engages in any of the commercial enterprise, such state Govt. shall be taxable as a person as far as income earned from such venture concerned.

Now let us discuss, one after the other, in detail, so that, we can able to understand much better about the "PERSON".

1) An individual :

The person who has to pay the tax "on his own income earned", during a particular year over and above the income ceiling under the Income-tax Act, which come into force from time to time, in the said particular year. Such, an individual has to be called as "PERSON" while computing the income. An individual means only human being and includes minor and person of unsound mind.

Example: Mr.B.Prathap, Shankarpally has earned an income of Rs.1,00,000/- during the year 2003-2004 from his salary. According to the Income Tax Act, in the Assessment year 2004-2005, if the income exceeds Rs.50,000/-, in such case, the incumbent has to file his income tax returns and to pay the tax, over the income ceiling. In this case, Mr.B.Prathap's income is more than the income ceiling. Hence, he may be called as an individual for computing the income tax.

2) An association of persons or a body of individuals whether incorporated or not :

In some cases, a few persons can form an association or a body and join together to perform a particular activity or business with a particular motive. And after fulfilling this objective, the persons are no more in the same organisation.

So, an association of persons or a body of individuals, whether incorporated or not, shall be treated as "person" for the computation of income tax over the income earned in a particular year.

Example : A) Joint venture

B) Trustees of a charitable Trust.

(The trustees activity is to be carry the objective of providing medical education, or general relief to the comparatively poor sections of society will be called activity carried on for charitable purpose provided the object is not to earn any profit).

3) A Hindu Undivided Family :

This type of families, we found mainly in India, rather than any country over the world.

"A Hindu undivided family is a family which enjoys the rights over the properties by all the said family members jointly and severally, and also which comes through their ancestors". Under the Hindu undivided Family the Head of the Family is called as "KARTHA" and the members of the family are to be called as co-parceners.

Under the Income Tax Act, 1961, the responsibility lies over he shoulders of "Kartha" of a Hindu Undivided family for the payment of Income Tax, on the earnings of the HUF, if it exceeds the income-tax ceiling.

A Hindu undivided family consists of all persons lineally descended from a common ancestor and includes their wives and unmarried daughters. So a Hindu undivided family is also to be called as a PERSON, while computing the income tax.

Example : M/s. Ramaiah & Sons, a Hindu undivided family has earned Rs.5,00,000/- as its income. The Kartha of the family is Sri.Ramaiah. Hence, for the computation of income-tax M/s. Ramaiah & Sons a HUF may be treated as a "PERSON".

4) A Firm :

If a firm functioning under the Indian partnership Act, 1932, whether registered or not, and earns the Income, in such case, the Firm has to pay the income tax over and above the income ceiling. So, as per the Income Tax Act, a Firm is also to be treated as "PERSON" in computing the income of its earnings for the tax purpose. A firm, which is a separate and distinct entity from its partners.

Example: M/s. Dhana Laxmi Traders of Vijayawada has earned an income of Rs.10,00,000/- during the year 1999-2000. The firm is to be treated as "person" for the computation of income.

5) A Company :

A company which incorporated under the Indian Companies Act, 1956, is also to be treated as "PERSON" while computing the income of its earnings for the tax purpose. A company with limited liability whether public or private and includes Indian and Foreign company. Even an unincorporated association may be taxed as a company if the Central Board of Direct Taxes (C.B.D.T.) issues an order to this effect.

Example: Hindustan Lever Ltd., has earned an income of Rs.20,00,000/- during the year 1999-2000, in such case, while computing his income of the company, the company is to be treated as "Person" for the tax purpose.

6) A Local Authority :

A local authority is also to be treated as a "person" while computing the income, as per the Income Tax Act.

Example: 1) Gram Panchayat 2) Municipal Council
3) Municipal Corporation 4) Mandal Panchayats etc.

7) Every artificial judicial (legal) person, not falling within any of the preceding sub-clauses :

Every artificial judicial person not falling within any of the preceding sub-clauses can also be called as a person.

Example: 1) Lord Sri. Venkateshwara Swami, Thirupathi.
2) Sri Gnyana Saraswathi, Basara etc.

8) A Statutory Corporation :

An establishment, an organisation incorporated under the statutory Act, by the Government, can also be treated as person for computing the income.

Example: 1) Industrial Finance Corporation of India
2) Andhra Pradesh State Road Tranport Corporation etc.

9) A state Government which carries or engages in any of the commercial enterprise, such state Govt. shall be taxable as a person on its earnings while computing the income.

Example: 1) Andhra Pradesh State Trading Corporation

So, the "person" is an "Assessee" for the payment of income tax, on his income earned during a particular year as per the Income Tax Act.

ASSESSMENT YEAR [Section 2(9)]

Under the Income Tax Act 1961, Section 2(9), "The Assessment year means the period of twelve months commencing on the 1st day of April every year and to be ended by 31st March of the immediate following year". The financial year of the Government of India is the Assessment year for all the categories of Assesses. And, it always starts from 1st April of a particular year and ends by 31st March of the immediate following year.

If we elaborate the Assessment year definition, the following points can be drawn.

1) It is the period of twelve months.
2) Commencing from the 1st April of a particular year and ends by 31st March of the immediate following year.
3) The financial year of the Govt. of India is the Assessment year for all the categories of Assessees and the period is similar to that of income tax Assessment year.
4) The Assessment year is also to be called as Income-Tax year.

Example: For the previous year 2003-2004 the Assessment year is 2004-2005.

The Assessment year is the year in which the income of the previous year is assessed to tax. Hence, it is a must to a person to know about the term "Assessment year". It is also called as tax year.

PREVIOUS YEAR [Section 3]

Income Tax Act, 1961 Section(3) deals with the previous year.

Previous year simply means the financial year of the Assessee immediately preceeding the Assessment year. In which income is earned.

Previous year is also known as ,
1) Accounting year
2) Income year

In a case of Commissioner of Income Tax Vs. Srinivasan & Gopalan, the Supreme Court has observed that previous year means "an accounting year comprised of a full period of 12 months adopted by an Assessee for maintaining his accounts. It is also further defined as a period of 12 months ending on or before 31st March of the relevant financial year in all the cases. Financial year ending March 31st will be the uniform previous year for all the tax payees. An Assessee who had his previous year ending on a date other than March 31st should close his books of accounts on March 31st every year.

In the case of a Business or profession newly set up or a source of income newly coming into existance, in any financial year, the previous year for the very first year shall be for the period beginning with the date of setting up of the business or profession or the date on which the source of income newly comes into existence and ending on the next March 31st of the said financial year.

There is no compulsion on any Assessee to close the Accounts on 31st March only. This section requires that for the purpose of Income-tax, income will have to be decided for the year ending 31st March every year. Therefore, though it would be convenient, both to the assessee as well as to the department, if the Assessee close their Accounts on 31st March. If for any reason, whether personal, religious or on any other ground, as assessee still wants to continue to close his accounts on a date different from 31st March, he can do so. In such a case, all that he would be required to do is to make his accounts on 31st March also, for the limited purpose of submitting the income-tax return.

Illustration 1: The income for the previous year" 1^{st} July, 1998 to 30^{th} June 1999" in the case of a newly set up business is to be assessed in which Assessment year ?

Solution	Previous year	Assessment year
	(1^{st} April to 31^{st} March)	(1^{st} April to 31^{st} March)
	In the illustration the previous year Starts from "1^{st} July, 2002 and ends by 30^{th} June, 2003". It means the financial year is ending by 30^{th} March, 2003 for this newly set up Business. Hence, the previous Year will be :	
	2003-2004	2004-2005

The previous year of a partner of a firm having no other income will be the same as that of the firm.

Illustration 2: What will be the Assessment years for the following Accounting years?

1) 1^{st} June 2003 to 31^{st} March 2004
2) 1^{st} April 2002 to 31^{st} March 2003
3) 13^{th} July 2001 to 31^{st} March, 2002
4) 11^{th} Nov. 2000 to 31^{st} March, 2001
5) 21^{st} Oct. 1999 to 31^{st} March, 2000.

Solution:

	Previous year	Assessment year
1)	2003-2004	2004-2005
2)	2002-2003	2003-2004
3)	2001-2002	2002-2003
4)	2000-2001	2001-2002
5)	1999-2000	2000-2001

NOTE: Though the business commences either on Dashahara or on Diwali, the Accounts should be closed by 31^{st} March only by every year.

EXCEPTIONS:

In general, the income earned during a previous year is taxed in its relevant Assessment year. But, there are certain exceptions to it. In the following cases, the income is being taxed in the same year in which it is earned.

1) Shipping Business income of non-resident ship owners.

Under section 172, the Shipping Business income of Non-Resident ship owners will not be allowed to leave the port till the tax on such income has been paid or alternative arrangements to pay the tax are made. So, in such cases the income is assessed to tax in the same current year.

2) In case of persons leaving India.

Under section 174, if a person leaves India with no intention to return, during the current Assessment year, the total income of such individual for the period between the expirty of last previous year and till the date of his departure, will be taxable in the current Assessment year.

3) In case of persons who are likely to transfer their assets to avoid tax.

Under section 175, if it appears that any person is likely to sell, transfer, dispose off or to part with any of his assets with an intention to avoid payment of any tax liability, in such cases, the Income Tax Officer, commences proceedings to assess the income for the period between the expiry of last previous years and the date of commencement of such proceedings.

4) In case of discontinued Business.

Under section 176, in case of discontinued Business or profession during any Assessment year the income of the period from the expirty of last previous year till the date of disconnection will be assessed to tax in the current assessment year.

PERMANENT ACCOUNT NUMBER

Under section 139A of Income Tax Act, 1961, the permanent Account number is a number which the Assessing Officer may allot to any person for the purpose of identification. So, such number is to be called as Permanent Account Number.

The Income Tax Officer is going to allot and give the permanent Account number to an Assessee soon after the filling of an application by an Assessee. In another words, every person who has taxable income and who has not been allotted any Permanent Account Number, shall apply to the Assessing Officer for allotment of a Permanent Account Number.

The Permanent Account Number, which helps to the income-tax authorities.

i) To know the previous years income and expenditure and the circulars issued there on by the income tax authorities to the Assessee and to assess the income accordingly.

ii) It helps the assessee for his future correspondence with the income-tax authorities. This number is to be mentioned for any type of correspondence with the Income-Tax Authorities.

It means that, an individual has to apply an application for the allotment of Permanent Account Number when the income earned by an assessee exceeds the tax limit.

Example 20: If Gross sales and Gross Receipts exceeds over and above Rs.50,000/- by an Assessee through his business and profession, in such cases the Assessee has to made an application for allotment of Permanent Account Number to the income tax authorities as per the Income-Tax Articles 139 and 114.

Similarly, every person carrying on business whose sales etc., are likely to exceed Rs.50,000/- in any year, and who hs not been allotted a Permanent Account Number, shall apply for the allotment of a Permanent Account Number.

The Assessing Officer, may also allot a Permanent Account Number to any other person, by whom tax is payable.

The Assessing Officer must be informed of any change in address or in the name and nature of business after a Permanent Account Number has been allotted. The person concerned shall quote the Permanent Account Number which has been allotted in all his returns to or correspondence with any Income-Tax authority in all challans for the payment of any sums due under the Act and in all documents relating to such transactions as may be prescribed in the interests of revenue.

SUMMARY

ASSESSEE :

- The concept of "Assessee" has ben defined under section 2, sub-section 7 of the Income Tax Act, 1961.
- Assessee means a person by whom any tax or any other sum of money is payable under this Act.

PERSON

- As per the Income Tax Act, 1961, under section (2) and sub section (3), the person includes :-
  - i) An individual.
  - ii) An association of persons or a body of individuals whether incorporated or not.
  - iii) A Hindu Undivided Family
  - iv) A Firm
  - v) A Company
  - vi) A Local Authority
  - vii) Every artificial judicial (Legal) person, not falling within any of the preceding sub-clauses.
  - viii) A statutory corporation
  - ix) A State Govt. which carries or engages in any of the commercial enterprise, such state Govt. shall be taxable as a person as far as income earned from such venture concerned.

ASSESSMENT YEAR

- Under the Income-Tax Act, 1961, section 2 (9) the Assessment year means the period of twelve months commencing on the 1st day of April every year and to be ended by 31st March of the immediate following year.
- The financial year of the Govt. of India is the Assessment year for all the categories of Assessee and the period is similar to that of Income-Tax Assessment year.
- The Assessment year is also to be called as Income-Tax year.

PREVIOUS YEAR

- Income-Tax Act, 1961, section (3) deals with the previous year.
- Previous year simply means the financial year of the Assessee of a full period of twelve months immediately preceding the Assessment year, ending on or before 31st March of the relevant financial year.
- In the previous year the Assessee earns the income.
- Previous year is also to be known as
  - i) Accounting year
  - ii) Income year

- The income earned during a previous year is taxed in its relevant Assessment year.

- In the following cases, the income is being taxed in the same year in which it is earned.
  - i) Shipping Business income of Non-Resident ship owners.
  - ii) In case of persons leaving India, with no intention to return.
  - iii) In case of persons who are likely to transfer their assets to avoid tax.
  - iv) In case of discontinued Business.

- Once the previous year adopted, cannot be changed.

PERMANENT ACCOUNT NUMBER

- Under Section 139A of Income Tax Act, 1961, the Permanent Account Number is the number which is to be given by the Income Tax Officer to an Assessee in order to identify the particular Assessee, such number is to be called as Permanent Account Number.
- It helps the Assessee for his future correspondence with the income tax authorities.

QUESTIONS

Short Questions:

1. Who is an “Assessee” ?
2. Define the term “person”.
3. Define the term “Assessment year”
4. What is “Previous year” ?
5. Previous year is also to be known as which year ?
6. Give any two examples of the income which is being taxed in the same year in which it is earned
7. What is Permanent Account Number (P.A.N.) ?
8. What is the Agricultural income ?
9. Under the Income Tax Act, 1961, Section 10 (1) whether the Agricultural income has been exempted from the payment of income tax or not ?
10. Whether the Agricultural income form part of total income of an Assessee or not?

Essay Type Questions :

1. What is meant by previous year ? What are the rules regarding determination of previous year for a continuing business and newly setup business, discontinued business.
2. “The Responsibility of payment of tax on income of an Assessee is depends upon his Residential sites” – Explain ?
3. Explain the term “person” with the suitable examples as per the Income-Tax Act?
4. Explain certain exceptions of income earned during a previous year is taxed in its relevant Assessment year ?

3. AGRICULTURAL INCOME

The term “Agricultural income” is one of the most important concept.

Under the Income Tax Act, 1961, Section 10(1), the Agricultural income has been exempted from the payment of income tax. And agricultural income does not form part of total income of an assessee.

Since, the inception of income tax in India, the Agricultural income had been totally exempted. Under the constitution of India, Article 270, the Government of India has to collect the tax on income other than the agricultural income. And as per the Indian Constitution, the agricultural income falls under the purview of State Governments to tax. And the State Government have been collecting the land revenue over the agricultural income.

But, from the assessment year 1974-75, the agricultural income is included in the total income of some non-corporate assessees for the rate purposes only, on the basis of the recommendation of Dr. Raj Committee.

Agricultural income is fully exempt from tax under section 10(1). However, it is taken for aggregation with other income for the purpose of calculating tax, where the total non-agricultural income exceeds Rs. 50,000/- for the asessment year 2000-2001.

Thereafter, the Assessee gets deduction from gross income tax calculated on the aggregate income as above, the income tax payable on the exempted income i.e agricultural income plus Rs. 50,000/- being basic exemption. The difference between the two calculations will be the tax payable by the Assessee. However, it cannot exceed 60% of the amount by which non-agricultural income exceeds Rs.50,000/-. More over, where non-agricultural income of an Assessee is less than Rs.50,000/- his agricultural income is not added with his non-agricultural income and therefore, such agricultural income is totally tax-free.

DEFINITION OF AGRICULTURAL INCOME [U/S 2(1)]

Under Section 2(1) of Income Tax Act, 1961, Agricultural income has been defined as,

1. “Any rent or revenue derived from land which is situated in India and is used for Agricultural purpose.

From the above definition, we can come to the conclusion that the Agricultural income means,

The income has to be related with the land or it should be derived from the land.

Examples:

a) Mr.Durkolla Narayana has got the income by giving the rights of cultivation to others of his own Agricultural land for Rs.10,000/-.
b) Mr. Kedarnath has received an income of Rs.15,000/- in the shape of revenue from his own agricultural land by performing Agricultural operations.

2. Any income derived from such land by
i) Agriculture, or
ii) The performance by a cultivator or receiver of rent-in-kind, of any process ordinarily employed by a cultivator or receiver of rent-in-kind to render the produce raised or received by him, fit to be taken to the market, or
iii) The sale by a cultivator or receiver of rent-in-kind in respect of which no process has been performed other than a process described in the paragraph; or

2. Any income derived from any building or any land with respect of which or the produce of which any process mentioned in (i) and (ii) above is carried on provided the following two conditions are fulfilled :-

   a) The Building is situated on or in the immediate vicinity of the land and is a building which the cultivator, or the receiver of rent-in-kind requires as dwelling house or as a store in kind requires as dwelling house or as a store house or other out building. The house must be needed by reason of its connection with land and
   b) The land is either assessed to land revenue in India or is subject to a local rate assessed and collected by the officers of the Government as such.

Where the land is not so assessed to land revenue or subject to a local rate, it must not be situated

i) In any area which is comprised within the jurisdiction of a Municipality etc, or a Contonment Board having a population of 10,000 or more as per last census, or

ii) In any area within such distance from the local limits of Municipality etc., as the Central Government may specify in this behalf in the official Gazette. This distance will not exceed eight kilometers and in determining the distance, the Government will be guided by the extent and scope for the urbanization of that area."

2. Such land has been used for Agricultural purposes.
It is necessary that income must be result of agricultural operations performed and agricultural land. Unless there is some measure of cultivation of land, some expenditure of human skill and labour upon its land can not be said to have been used for agricultural purposes. Agriculture means performance of basic operations – ploughing, sowing irrigating and harvesting.
Example : Mr.Sheshavatharam, has got an income of Rs.5,000/- from his own agricultural land by performing the Agricultural operations like ploughing, sowing, watering etc. and employed some sort of human skill, labour, energy.

3. The land is to be situated in India.
Example : If an Indian citizen owns land in Bangladesh and this land is being cultivated by some one in Bangladesh, the rent received from such land will not be treated as Agricultural income for tax purposes. Such, income is to be taxable under the head of "Income from other sources". If the land is situated in India, in such case it will become as an agricultural income.

The compensation received from the Govt. for taking over of a plot of land being used for Agricultural purposes, will not be treated as an Agricultural income.

If the tenant does not pay the rent of land and allows it to accumulate, and any interest payable on such amount will also not to be considered as an agricultural income.

If a merchant purchases standing crops and sells them at profit, such a profit cannot be branded as an Agricultural income simply on the ground that there is no Agricultural operations at all like ploughing, sowing, planting, watering, harvesting etc.

KINDS OF AGRICULTURAL INCOME [U/S 2(1)]

In the earlier chapter, we have discussed about the meaning of the Agricultural income. Now, let us know the kinds of agricultural income in this unit.

The kinds of Agricultural income are as follows under the Income Tax Act, 1961, section 2(1).

KINDS OF AGRICULTURAL INCOME

- Any amount received as rent, or revenue from such land.
- Income derived from Agriculture
- Any income accruing to the person by the performance of any process to render the produce marketable
- Any income received by the person by the sale of produce raised or received as rent-in-kind
- Income from buildings used for agricultural purpose.

Now, let us discuss about the each kind of Agricultural income one after the other.

1. Any amount received as rent, or revenue from such land :

First, let us know the meaning of rent or revenue from the land.

“Rent can be defined as a payment in cash or in kind which the owner of the land receives from the another person in consideration of a grant of a right to use land for the certain period”.

In some or the other reason, the owner of the land may not perform agricultural operations by himself, but gives his land on contract basis for any consideration, either in cash or in kind. Such an amount received from the actual cultivator by the owner of the land shall be Agricultural income.

"The Revenue is in the sense, income other than rent and that is why mutation fees received from the tenants on their getting occupancy holdings and the fees paid by the tenants at the time of renewal of their lease".

The Revenue is to be derived from land only, if the land is immediate and effective source of the revenue and not the secondary and indirect source. So, any income or revenue which indirectly derives from the land cannot be presumed to be the agricultural income.

The Supreme Court has clearly clarified in a case Bacha Guzder vs. Commissioner of Income Tax, that dividend paid by a company to its share holders out of its agricultural income is not an income derived from land. So, it is the share holding in the company and not the land. And it is also clearly clarified that the interest on arrears of rent payable inrespect of agricultural land cannot be agricultural income. Because, it is neither "rent" nor "revenue" derived from land.

Example 1: Sri. M.Narayana Bichkundekar is having the Agricultural land. But, he himself unable to perform the agricultural operation of his own. So, he has given his land on contract basis for cash/kind for an amount of Rs.10,000/- so, the amount received on such consideration by the owner from the actual cultivator shall be an agricultural income.

2: **Income derived from Agriculture**: Income derived from the land situated in India by applying agricultural operation shall be treated as an Agricultural income.

Agricultural operation includes, sowing, planting, watering, harvesting etc. So, any income resulting from such operations shall be an Agricultural income.

Agricultural income also includes income from orchards or from horticulture and floriculture.

2. If the income derived by, without any agricultural operations, such an income although derived from land cannot become agricultural income.

Example 1: Grass, Trees etc. have grown spontaneously i.e. without any help of human skill, effort, labour etc. In such cases, the income resulting from the sale of such grass, trees or lease rent of such land shall not be agricultural income.

2: Income from poultry and dairy farming, fisheries, mining, stone quarries, breeding and rearing of live stock, all these incomes although remotely linked with land but cannot be called as an agricultural income. Because there is no cultivation at all and there is no agricultural operations too.

3: Sri Ram Gopal Kothwal has solely involved in Agriculture in his own Agricultural land with all the agricultural operations. And get the produce i.e. kind worth Rs. 10,000/-. Hence, it shall be called as agricultural income.

3. Any income accruing to the person by the performance of any process to render the produce marketable.

The owner, cultivator or the land lord who receives the produce as rent-in-kind, and any income derived from such a process shall be agricultural income. Such a process shall be agricultural income. Such a process must be employed to render the produce fit for marketing. But, one thing we have to remember is that the produce should not change its original character inspite of the processing unless the produce cannot be sold in that form or condition. The process may be either manual or mechanical.

Example 1: Tobacco leaves, to be dried to make them suitable for the market and thus profit earned by selling dried tobacco shall be agricultural income.

Example 2: Unginned cotton can be sold in its original form. And if ginning operation takes place and any profit is attributable, such a profit shall not be agricultural income. Because, the ginning operation is not a must to render the produce fit to be taken to the market.

4. Any income received by the person, by the sale of produce raised or received as rent-in-kind.

Any income received by any person on the sale of agricultural produce raised by him or received as rent-in-kind on lease, such income shall be agricultural income. If the person sells the produce by establishing his own selling shops and receives any extra profit thereon due to shopping activities shall not be agricultural income.

Example 1: Sri. Sangameshwar of Shankarampet(A) has sold his agricultural produce raised by him for Rs. 10,000/-. So, it is an agricultural income of Sri. Sangameshwar.

Example 2: Sri. Babu Rao Uppalwar of Degloor, has received as rent-in-kind worth Rs.10,000/- from his own agricultural land. So, it will become as an agricultural income of Sri. Babu Rao.

5. Income from Buildings used for Agriculture :

Income derived from a building used for agricultural operations shall be agricultural income provided :

i. The building from where the income is received is in the immediate vicinity of the land and is occupied by the owner or by the cultivator or by the receiver of rent-in-kind.
ii. The building is used as a dwelling house or a store house or other out house for agricultural operations and which is nearer to the agricultural land.
iii. The land in which the building is situated the land is assessed to land revenue in India.
iv. The building should be 8 kms. away from the urban area or the Municipality area.
v. The population in the said area does not exceed 10,000.

Thus, there are various kinds of Agricultural income in existence.

PARTIALLY AGRICULTURAL AND PARTIALLY NON-AGRICULTURAL INCOME

There are certain incomes which are neither wholly agricultural in nature nor can they be said to arise from business. Such income comprises of both agricultural as well as nor agricultural income. In such a situations it is necessary to divide such income two parts – Agricultural income and non agricultural income. The assessee has to prove any income or part of the income, is agricultural income. These cases have been dealt within the Income Tax Act., Rules 1962, under Rules No. 7 and 8given below.

RULE 7 OF INCOME TAX RULES 1962

Under rule 7 the market value of the agricultural produce raised by the assesse or received as rent in kind and utilised as raw material will be deducted out of total profit of such business. This rule is applicable in case of cotton, tobacco, sugar cane etc.,

Example-1: M/s. Bhagya Laxmi Khandasari Sugars (Pvt.) Ltd. Banswada, Nizamabad Dist. has its own agricultural land. The Sugar cane be produced in the said agricultural land is being utilized as raw material to the said industry.

In such case, the sugar cane produced from the agiruclural land is to be treated as an agricultural income. And, for the calculations of Sugar cane worth, the market value of the produce is to be taken into consideration, depending upon the value in the previous year.

If the produce is not sold in raw state, the cost of cultivation, land revenue paid or the rent of land and an element of profit as permitted by Income Tax Officer, all these added together will constitute market value.

The sugar produced and sold, and the profit earned thereon comes under the income source of Business and profession.

Hence, M/s. Bhagya Laxmi Khandasari Sugar Pvt. Ltd., has to show its income separately as agricultural income and non-agricultural income.

The total agricultural income raised by an assessee out of his own agricultural land or through the land on lease and received as the rent in kind there on is totally eligible for deduction from the assesses total income.

But, in the above said example, if an assessee incurs any expenditure on agriculture, then, such an expenditure is not eligible for deduction.

The Rule 8 of the Income Tax Rules, 1962, deals with the Income from manufacture of Tea. It involves two types of operations.

1) Agricultural operations : sowing, planting, watering etc.
2) Industrial Operations : Blending of Tea

In such case, Income Tax Act provides that 60% of income of a Tea business will be agricultural income and 40% of income will be chargeable to tax under “profits and gains of Business or profession”. This rule applies only in the case where the assessee himself grows the leaves and manufactures tea in India.

The cost of planting bushes in replacement of bushes that have died will be taken into consideration and an allowance shall be made, while computing such income.

It is the responsibility of the assessee to prove whether a particular income is agricultural income or bushes income. The assessee has to satisfy the income tax authorities in this regard.

Example-1: Mr. M.Sangameshwar has earned an income of Rs.10,000/- from tea plantation and tea industry by agricultural and industrial operations too.

Hence, out of his total income Rs.6,000/- will become as an agricultural income and Rs.4000/- will become as an income from Business, i.e. 60% and 40% of his total income as per the income tax act rules.

Non Agricultural Incomes related to land :

The following incomes are not the agricultural incomes though which relates with the agricultural land and derives the income with the agricultural land.

1. Income derived by the brick-making.
2. Income from pots making.
3. Income from markets, fisheries, etc.
4. Income from the supply of water for irrigation pruposes.
5. Income from mining royalties.
6. Income from forest trees of spontaneous growth by the sale of wood bark, leaves, fruit, etc.
7. Income from stone quarries.
8. Income from dairy.
9. Income from poultry farming.
10. Income or any consideration received by the sale of Agricultural land for its possession either by the Govt. or by any other person.
11. Interest received on the agricultural loans either in cash or in kind.
12. Commission received by the landlord on the sale of produce of a tenant.
13. Income received from the maintenance of markets.
14. Income or consideration received on transfer of Agricultural land.
15. Income received from the maintenance of cattle irrespective of agriculture.

Treatment of Agricultural Income for Tax purpose

The Central Government made it mandatory, from the assessment year 1974-75 onwards, that the net agricultural income is to be added to the total non-agricultural income computed as per the Income Tax Act, for the purpose of determining the income tax on the non-agricultural income, although the agricultural income will remain fully exempt. The integration is done only in those cases where an assessee has both agricultural and non-agricultural incomes.

Non-agricultural income is the computed total income of an assessee as per the provisions of the Income Tax Act, 1961. The Net Agricultural Income is the aggregate of the agricultural income computed in accordance with the rules laid down under section 2(1A) of the Income Tax Act, 1961 and rules 7 and 8 of the Income Tax Rules, 1962. These Rules include :

1. Rent or revenue derived from agricultural land to be computed on the same basis as adopted for computation of income under the head "income from other sources" under sections 57 to 59 of the Income Tax Act.

2. Income derived from agricultural operations to be computed on the same basis as adopted for computation of income under the head "profits and gains of business or profession". All the provisions of sections 30, 31, 32, 34, 36, 37, 38, 40, 40A, 41, 43 and 43A of the Act shall be applicable, including the provisions of depreciation and loss in the case of death of animals used in agricultural operations.

3. Income derived from agricultural house property to be computed on the same basis as adopted for computation of income under the head "income from house property" under sections 23 to 27 of the Income Tax Act.

4. For computing share of income from tea business income, the provisions of rule 8 shall be applicable.

5. For share of income or loss of a partner from the agricultural income or loss of a firm assessed as firm, the rules as are provided in Income Tax Act for computing the share of profits or losses from a firm assessed as firm shall be applicable.

6. Loss incurred in agriculture shall be allowed to be set off only against gains from agriculture. The share of loss of partner from a firm assessed as AOP *shall not* be allowed to be set off from his own agricultural income.

7. If the State Government levies any tax on Agriculture, it is allowed as deduction from such income.

8. Where the net result of agricultural income from the various sources stated above in a particular previous year is loss, then such loss shall be disregarded and net agricultural income shall be taken to be *nil*.

Thus, agricultural income becomes a factor in determining the tax on the non-agricultural income of a person, subject to the fulfillment of ALL the following conditions:

a. The assessee must be an Individual, HUF, Association of Persons or Body of Individuals, or an Artificial Juridical Person.
b. The assessee should have net agricultural income exceeding Rs.5,000 during the relevant previous year.
c. The amount of non-agricultural income, during the relevant previous year, should exceed the maximum tax-free amount of Rs.50,000 in the case of assessees mentioned in (a) above.

If any of the above condition is not fulfilled, then the agricultural income cannot be integrated with the non-agricultural income.

Illustration – 1

Compute the tax liability in each of the following cases for the assessment year 2004-05:

a. Mr. A's total income from all other sources is Rs. 34,000 and net agricultural income is Rs. 1,00,000
b. Mr.D's total income from all sources is Rs. 56,000 and net agricultural income is Rs. 10,000
c. Mr. X's total income of Rs. 1,04,000 and net agricultural income of Rs. 10,000
d. A HUF has total income of Rs. 3,24,000 and net agricultural income of Rs. 1,00,000
e. Mr. Kumar's total income from all sources is Rs. 8,60,000 and net agricultural income of Rs. 1,50,000

Solution

In this problem, except in case a, in all other cases , all the three conditions are fulfilled. Hence integration of agricultural and non- agricultural incomes is to be made in all cases except in case a.

Case a

There is no tax liability in this case, as the non- agricultural income does not exceed the basic exemption limit of Rs. 50,000.

In all the other cases, as the conditions are fulfilled, the agricultural and nonagricultural incomes are integrated and the tax liability is computed as follows:

Case b

Step	Particulars	Rs.	Rs.
1	Add agricultural income and non-agricultural income (Rs. 10,000 + Rs. 56,000)	66,000	
2	Tax on the total as per step 1		2,200
3	Add agricultural income and basic exemption limit (Rs. 10,000 + Rs. 50,000)	60,000	
4	Tax on the total as per step 3		1,000
5	Different tax		1,200
6	Deduct rebates		Nil
7	Add surcharge		Nil
	Balance tax payable		1,200

Case c

Step	Particulars	Rs.	Rs.
1	Add agricultural income and non-n agricultural Income (Rs. 10,000+Rs. 1,04,000)	1,14,000	
2	Tax on the total as per step 1		11,800
3	Add agricultural income and basic exemption limit (Rs. 10,000 + Rs. 50,000)	60,000	
4	Tax on the total as per step 3		1,000
5	Different tax		10,800
6	Deduct rebates		Nil
7	Add surcharge		Nil
	Balance tax payable		1,200

Case d

Step	Particulars	Rs.	Rs.
1	Add agricultural income and non-agricultural income (Rs. 10,000 + Rs. 3,24,000)	4,24,400	
2	Tax on the total as per step 1		1,01,200
3	Add agricultural income and basic exemption limit (Rs. 10,000 + Rs. 50,000)	1,50,000	
4	Tax on the total as per step 3		19,000
5	Different tax		82,200
6	Deduct rebates		Nil
7	Add surcharge		Nil
	Balance tax payable		82,200

Case e

Step	Particulars	Rs.	Rs.
1	Add agricultural income and non-agricultural income (Rs. 1,50,000 + Rs. 8,60,000)	10,10,00	
2	Tax on the total as per step 1		2,77,200
3	Add agricultural income and basic exemption limit (Rs. 10,000 + Rs. 50,000)	2,00,000	
4	Tax on the total as per step 3		34,000
5	Different tax		2,43,000
6	Deduct rebates		Nil
7	Add surcharge @ 10% on Rs. 2,43,000		24,300
	Balance tax payable		2,67,300

Illustration –2

Compute the tax liability of Mr. Sharma for the assessment year 2004-05

a.	Rent of agricultural land	60,000
	Land revenue taken to purchase agricultural land	6,000
	Interest on loan taken on recovery of agricultural rent	10,000
	Collection charges on recovery of agricultural rent	1,000
b.	Interest on arrears of land revenue received from tenants	50,000
c.	Income from manufacturing business carried on	50,000

Solution

Computation of Agricultural Income

	Rs	Rs	
Rent of agricultural land		60,000	
Less expenses incurred:			
			Land revenue
			6,000
Interest on loan	10,000		
Collection charges	1,000		
Net agricultural income		17,000	
		43,000	

COMPUTATION OF NON-AGRICULTURAL INCOME

	Rs
Income from manufacturing business	50,000
Interest on arrears of land revenue	12,000
Non-agricultural income	**62,000**

COMPUTATION OF TAX LIABILITY

Step	Particulars	Rs.	Rs.
1	Add agricultural income and non-agricultural income (Rs. 43,000 + Rs. 62,000)	10,10,00	
2	Tax on the total as per step 1		10,000
3	Add agricultural income and basic exemption limit (Rs. 43,000 + Rs. 50,000)	93,000	
4	Tax on the total as per step 3		7,600
5	Different tax		2,400
6	Deduct rebates		Nil
7	Add surcharge		Nil
	Balance tax payable		2,400

SUMMARY

DEFINITION OF AGRICULTURAL INCOME

- Under Section 2(1) of Income Tax Act, 1961, Agricultural Income has been defined.

- The Agricultural income
-
  i. The income has to be related to the land.
  ii. Such land has been used for Agricultural purposes.
  iii. The land should be situated in India.

- Such an income cannot be branded as an Agricultural income, when there is no Agricultural operations.

- Agricultural operations means, ploughing, sowing, planting, watering, harvesting etc.

KINDS OF AGRICULTURAL INCOME

- Under the Income Tax Act, 1961, Section 2(1) the kinds of Agricultural incomes are:
  i. Any amount received as rent, or revenue from such land.
  ii. Income derived from Agriculture.
  iii. Any income accruing to the person by the performance of any process to render the produce marketable.
  iv. Any income received by the person by the sale of produce raised or received as rent-in-kind.
  v. Income from Buildings used for Agricultural purpose.

- Agricultural income also includes income from orchards or from Horticulture and Floriculture.

- The income derived by without any Agricultural operations, such an income although derived from land cannot become Agricultural income.

- The owner, cultivator or the land lord who receives the produce as rent-in-kind, and any income derived from such a process shall be Agricultural income. And the produce should not change its original character and it should be fit for marketing.

- Unginned cotton is an Agricultural income and Ginned Cotton is not an Agricultural income as profit is attributable by ginning operation.

- Any income received by any person on the sale of Agricultural produce raised by him or received as rent-in-kind on lease, such income shall be an Agricultural income.

- If the person sells the produce by establishing his own selling shops and receives any extra profit thereon due to shopping activities shall not be an Agricultural income.

- Income from buildings used for Agriculture, can be called as an Agricultural income only when the building from where the income as received is in the immediate vicinity of the land and is occupied by the owner or by the cultivator or by the receiver of rent-in-kind.

- It should be called as an Agricultural income only when the building is used as a dwelling house or a store house or other out building for Agricultural operations and which is nearer to the Agricultural land.

- The land should be assessed for land revenue in India.

- The Building should be 8 kms. away from the urban area or the municipal area.

- Unginned cotton is an Agricultural income and Ginned Cotton is not an Agricultural income as profit is attributable by ginning operation.

- Any income received by any person on the sale of Agricultural produce raised by him or received as rent-in-kind on lease, such income shall be an Agricultural income.

- If the person sells the produce by establishing his own selling shops and receives any extra profit thereon due to shopping activities shall not be an Agricultural income.

- Income from buildings used for Agriculture, can be called as an Agricultural income only when the building from where the income as received is in the immediate vicinity of the land and is occupied by the owner or by the cultivator or by the receiver of rent-in-kind.

- It should be called as an Agricultural income only when the building is used as a dwelling house or a store house or other out building for Agricultural operations and which is nearer to the Agricultural land.

- The land should be assessed for land revenue in India.

- The Building should be 8 kms. away from the urban area or the municipal area.

- The population in the said Area does not exceed 10,000.

PARTIALLY AGRICULTURAL AND PARTIALLY NON-AGRICULTURAL INCOME

Some times income comprises of both agricultural as well as non-agricultural income. In such cases it is necessary to divide such income into two parts

a) Agricultural income and (b) non-agricultural income.

Rules No. 7 & 8 of Income Tax Rules 1962 deals with the partially agricultural income.

- Any non-agricultural income which includes partly or thereon in the agricultural income, is to be called as partially agricultural income.
- The rule 8 of the Income Tax Rules 1962 deals with the income from manufacture of tea.
- It involves two types of operations.
  - i) Agricultural operations. Examples Sowing, planting, watering etc.
  - ii) Industrial operations. Example: Blending etc.
- In such cases Income Tax Act provides that 60% of income of a Tea Business will be an Agricultural income and 40% of income will be chargeable to tax under "profit and gains of Business or profession".
- This Rule applies only in the case where the Assessee himself grows Tea leaves and manufactures Tea leaves in India.
- It is the responsibility of an Assessee to prove whether a particular income is agricultural income or business income. The Assessee has to satisfy the income tax authorities in this regard.
- Some of the incomes which derives and related to land are not to be called as Agricultural incomes.
  Examples: 1) Income derived by the Brick making.
  2) Income from Dairy etc.

QUESTIONS

Short Questions

1. What is the Agricultural Income ?
2. Under the Income Tax Act, 1961, Section 10 (1) whether the Agricultural income has been exempted from the payment of Income Tax or not ?
3. Whether the Agricultural income form part of total income of an Assessee or not ?
4. The revenue which is being collected by the Stage Governments over the Agricultural income is to be called as which revenue ?
5. What is the recommendation of Dr. Raj Committee on Agricultural income ?
6. What is meant by an Agricultural operations ?

7. What is meant by a Non-Agricultural income ?
8. What is meant by a partially Agricultural income ?
9. How is the income from manufacture of Tea is Taxable under Rule 8 of Income-Tax Rules ?
10. Give any two examples of non agricultural incomes related to land ?

ESSAY TYPE QUESTION :

1. Define the Agricultural income under the section 2(1) of Income-Tax Act, 1961.
2. Explain the kinds of Agricultural income.
3. Explain the income from buildings used for Agriculture.
4. Explain in detail about the partially Agricultural and partially Non-Agricultural incomes with suitable examples ?

PROBLEMS/PRACTICALS

1. Sri Nilakantam Pandurangam of Shankarampet (A), has received an income of Rs.20,000/- by giving the rights of cultivation to Sri. Malla Reddy of his own Agricultural land. Whether it is an Agricultural income or not - explain ?
2. Sri. Nagappa of Alladurg has got income of Rs.10,000/-. The income has been fully derived on lease from his own Agricultural land. So, whether it is to be treated as an Agricultural income or not, as per the Income Tax Act, 1961 – Explain ?
3. Sri. Prabhakar of Kurnool is having an Agricultural land. He has received an income of Rs.25,000/- on it, by using for Agricultural purposes. So, explain which type of income it is ?
4. Sri. Khaja Mahamood Ahmed of Hyderabad is having an Agricultural land at Pakistan. He has given this land to a cultivator of Pakistan and received an income of Rs.30,000/-. Whether, it is an Agricultural income or not – Explain ?
5. Sri Vinay Kumar of Hyderabad is having the Agricultural land in Medak District. From this agricultural land he has received an income of Rs.20,000/- by performing agricultural operations. So, explain which type of income is it ?
6. Sri. Narayankhed Veera Reddy is having the Agricultural land in the Singoor village. The Govt. have paid the compensation for taking over of land being used for Agricultural purposes. So, whether it is to be called as an Agricultural income or not ?
7. Sri. M.Baga Reddy and Sri. M. Veera Reddy together the cotton merchants have purchased the standing crop from Sri.T.Krishna Reddy, Agriculturist for Rs.1,00,000/-. And they sold the crop for Rs.1,50,000/-. So, explain whether the profit earned by them is an Agricultural income or not ?
8. Explain whether the following incomes are Agricultural income or not ?
   i) Income received through dairy related to Agricultural land.
   ii) Income received from dairy without connection with the Agricultural land.
   iii) Income received by a land lord through dried Tobacco.
   iv) Income received by a merchant through dried Tobacco.
   v) Income received by the sale of gross which has grown spontaneously.
   vi) The compensation received in connection with the natural calamity by a farmer from Insurance co.
   vii) Income received from commercial crops in India.

Answer to the Problems/Practicals :

1. Agricultural income.
2. Agricultural income.
3. Agricultural income.
4. No, it is not an Agricultural income. Because, the land is situated in outside India.
5. Agricultural income.
6. It is not to be called as an Agricultural income. Because, the income was not derived through the Agricultural operations.
7. It cannot be branded as Agricultural income, simply, on the ground that there is no Agricultural operations.
8.
    i) Agricultural income.
    ii) Non-Agricultural income.
    iii) Agricultural Income.
    iv) Non-Agricultural income.
    v) Non-Agricultural income.
    vi) Agricultural income. Because, the Govt. is not taking over the land on compensation. It is only the compensation given to the farmer in order to meet the loss against natural calamity.
    vii) Agricultural income.
9. Discuss whether the following items of income constitute 'agricultural income' for the purpose of the Act.
    a) Income derived from rubber plantation in Singapore.
    b) Rent received from a tenant to whom land in India has been let out and who uses it for cultivating wheat.
    c) Dividend received by a shareholder from an Indian company the whole of whose income is agricultural income.
    d) Income derived from sale of timber of spontaneous growth on Indian soil.

    [Ans. Yes (b), No (a), (c) and (d)]
10. State whether the following are agricultural income?
    a) An assessee earns Rs.10,000 as interest on his capital for selling the agricultural produce of his tenants.
    b) A partner received Rs.10,000 as interest on his capital from the firm engaged in agricultural operations.
    c) An assessee earns Rs.40,000 on the sale of Khandsari made from the sugarcane grown on an agricultural land owned by him.
    d) Compensation received from an insurance company for damage of crop.

    [Ans. Yes (b), (c) and (d) No (a)]

4. INCOME MEANING AND DEFINITION

The word income is very important concept. It is very much essential to a person, Business organisation and also to the Government in order to meet the regular and routine expenditure. If there is no income, the question of meeting the expenditure becomes very difficult. In such cases, we have to go for the loans. And now the question arises about the loan repayment. Even to repay the loan, one should plan for the income resource. It all applicable to the person, business organisation, and also to the Government.

Now, let us discuss, the term “income” from the Governments point of view. The Government is going to get the income by imposing the various taxes. One among the various taxes is income tax. Every Government activity depends upon the “income of the Government”.

An individual a firm, a business organiation is going to earn the income through one or the other activity. So, it is quite clear that, the income is going to play a predominent role in the society with all the above stated reasons. Hence, it is a must for us to know about the meaning and definition of the income. Since, income tax is a tax on income, it becomes very important to understand the concept of income.

Meaning of Income :

In general tem “income” means any monetory gain either in the form of money or money’s worth coming from a certain source with some sort of regularity.

In another sense, the income means the return on investment (ROI).

In Oxford Dictionary meaning of the term “income” is “periodical receipts from one’s business, land, work, investments, etc.”

Important features of Income :

1. Income is linked with the source.
2. Income must come from outside. For example:
    i) income received from transactions between a Branch office and
    ii) Head Office and subscriptions received by a club from its members is not income.
3. Income is being received by any source whether legal or illegal and taxable over the income ceiling.
4. The income may be received either in the form of money or money’s worth.

Definition of Income :

Income Tax Act 1961, Section 2(24) defines the term “Income” as :

"Income includes"

i. Profit and gains
ii. Dividend
iii. Any voluntary contributions received by a charitable or religious trust or other institution (Except in case where such contributions have been received with a specific direction that these sums would form past of the corpus of the trust or institution).
iii(a) Any special allowance or benefit, other than perquisite included under sub-clause (iii), 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.
iii(b) 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,
iv. Any perquisite or profit in lieu of salary taxable under section 17(2) or (3).
iv(a) Value of any benefit or amenity, whether convertible into money or not, obtained by a representative assessee or by any person on whose behalf such benefit is received by representative assessee ;
v. The value of any benefit or perquisite allowed to director or a person substantially interested or their relatives;
vi. Any sum chargeable to income tax under clauses (ii) and (iii) of section 28 or under section 41 or 59.
vii. The value of any benefit or perquisite taxable under section 28 (iv).
viii. Any capital gains taxable under section 45;
ix. The profits and gains of any business of insurance carried on by a mutual insurance company or by a cooperative 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.
x. Profits on sale of license granted under the Imports (Control) Order 1955 under section 28 (iii a);
xi. Any cash assistance received or receivable by any person against exports under any scheme of the Central Government under section 28 (iii b);
xii. Any duty of customs or excise repaid or repayable as drawn back to any person against exports under section 28 (iii c);
xiii. Any winnings from lotteries, cross word puzzles, races including horse races, card game and other games of any sort or from gambling or batting of any form or nature whatsoever;
xiv. Any annuity due or commuted value or any annuity paid under the provisions of section 280 D;
xv. Any sum received by the assessee from his employees as contributions to any provident fund or superannuation fund or any fund set up under the provisions of the employees state insurance act, 1948 or any other fund for the welfare of such employees.

The above mentioned definition does not give its definition but widens the scope of the term "income". It simply tells us the sources and the income of which is incuded in the scope of income chargeable to tax.

According to the decision of the Privy Council, in Commissioner of Income Tax, Bengal vs. Shaw Wallace & Co. Ltd., "income" cannotes a periodical monetary return coming in with some sort of regularity or expected regularity from definite sources which need not be continuously productive, but their object must be the production of a definite return as distinguished from a mere windfall.

Thus, the meaning and definition of the income is very broad, like a fruit of a tree or crop of the field where the source is a must in both the cases alike.

GROSS TOTAL INCOME

Gross total income of an assessee consists of:-

1. Income from salaries (section's 15 to 17).
2. Income from House property (section's 22 to 27).
3. Profits and Gains of Business or Profession (section's 28 to 44).
4. Capital Gains (section's 45 to 55) and
5. Income from other sources (section's 56 to 59) of Income Tax Act, 1961.

First of all, we have to compute the taxable income of an assessee under Head-wise separately. In order to calculate the taxable income under each head certain deductions have to be made from the Gross income of that head. These deductions are different for each head.

Then, after computing the head wise income separately, these incomes should be added together to find out the Gross Total Income of the Assessee. Gross total = (income from salaries + Income from House Property + Income from profits & gains of business or profession + Income from capital gains + Income from other sources + Income of other persons to be included in Assessess income).

Thus, the gross income of an assessee may be calculated.

TOTAL INCOME

Total Income = (Gross Total Income – Deduction Allowed under Section 80D to 80U
Section 14 of the Income-Tax Act, 1961 deals with the total income of an Assessee.
In order to derive the total income of an Assessee the following steps are to be followed.

- i) Head-wise income should be computed.
- ii) Admissible head-wise deductions are to be considered.
- iii) Add together all the Head-wise incomes to get Gross Total income.
- iv) From the gross total Income certain deductions are to be allowed under section 80D to 80U.
- v) The Net-amount, thus arrived, is a total income of an Assessee.

It should be rounded off to the nearest multiple of Rs.10/-.

TAXABLE INCOME

The income of an assessee should fall under any of the below stated heads for the computation of taxable income.

1) Income from salaries
2) Income from House property
3) Profits and Gains of Business or Profession
4) Capital gains
5) Income from other sources.

Any income which cannot come and to be included under any of the above first four heads should be included under "Income from other sources".

First we have to find out the total income of an assessee head wise, separately, by allowing certain deductions admissible under each head from the Gross income of that head.

In addition, to that certain deductions are also allowed under section 10, to compute the taxable income under different heads.

After computing the head wise income separately, these should be added together to find out the Gross Total income of the Assessee. Afterwards, again certain other deductions are allowed under section 80D to 80U from this Gross total income. The net amount thus arrived at, after those deductions from the Gross total income is known as "Taxable Income".

Thus, the taxable income may be calculated of an assessee.

CASUAL INCOME [(U/S 10(3)]

Casual income is that income, the receipt of which is accidental and without any stipulation. It is in the nature of unexpected wind fall.

Examples-1: Any money or valuable articles found lying on the road.
2: Gifts received from friends and relatives on the occasion of birthday or wedding anniversary etc.
3: Gift or Award received for tracing out something etc.

Under section 10(3), casual income includes,

1. Any receipt which are of a casual and non-recurring or a temporary nature, including winning from lotteries, card games, horse races etc.
2. Casual incomes are exempted up to a total of Rs. 5,000 in previous year and in the case of winning from horse races the exemption is Rs. 2,500. Excess if any is taxable under the head income from other sources. The maximum exemption is only Rs. 5,000 but not Rs. 7,500.

But, casual income does not include,

1. Capital gains or,
2. Receipts arising from business or the exercise of a profession or occupation, or,
3. Receipts by way of addition to remuneration of an employee such as bonus, gratuity, perquisite etc.
4. Voluntary payments received in exercise of an occupation are not to be treated as casual income.

Examples :

1. Tips given to hotel bearer.
2. A regular allowance given every year as a voluntary gift by the parent to a child.
3. A regular allowance given year after the year purely as a voluntary gift by a husband to his wife.
4. A regular allowance given year after year purely as a voluntary gift by one relation to another.

CAPITAL AND REVENUE : INCOME, EXPENDITURE

Income tax is a tax on income but all incomes are not taxable. Under the Income Tax Act, only revenue receipts are taxable. However, capital gains are taxable at special rates. In other words, revenue receipt is treated as income and it is taxed and not the capital receipt.

The revenue expenditure is allowed as deduction while computing net profits and gains of a business or profession whereas the capital expenditure is allowed. Therefore, we must know the distinction between capital and revenue.

CAPITAL AND REVENUE

- Receipts
  - Revenue Receipts (Treated as income)
  - Capital Receipts (Not treated as income)
- Expenditure
  - Revenue Expenditure (Allowed to be deducted while computing the profits of a business or profession)
  - Capital Expenditure (Not allowed to be dedu-cted).

In the income Tax Act, no where these two terms are clearly defined and the Act does not make any clear distinction between them. But to determine the tax liability of an assessee it is very important to know the differences between them. As the Act does not make a clear distinction. The judgements of the various courts on different occasions and Accounting principles should be taken as the basis to make a clear demarcation between them.

CAPITAL INCOME

Capital incomes are also known as capital receipts. Unlike revenue receipts capital receipts are not taxable. Therefore, we have to know, the meaning of a capital income.

An income which is not casual and non-recurring in nature is known as a capital income. Therefore the capital income is not a regular income of a business. It comes to the business now and then.

Example-1) Sale proceeds of fixed assets such as land & buildings, Machinery, Furniture etc.
2) Compensation received for Nationalisation.
3) Money received on the issue of shares.
4) Insurance claim in respect of a fixed asset.

REVENUE INCOME

Revenue income is also known as Revenue receipt. Under the Act, revenue receipt is considered as income and hence taxable. Therefore, we must know the meaning of a Revenue Income.

An income which is regular or usual and recurring in nature is known as a Revenue Income.

In other words, it is a regular income of a business unlike capital income.

Example-1) Sale proceeds of goods.
2) Sale proceeds of a building by an estate dealer.
3) Money received on the sale of shares by a stock broker.
4) Insurance claim in respect of a stock-in-trade.

RECEIPTS

The difference between capital and Revenue receipts :

	Capital Receipts		Revenue Receipts
1.	Any receipt which is casual and non-recurring in nature is called a capital receipt.	1.	Any receipt which is regular and recurring in nature is Called a Revenue receipt.
2.	Sale proceeds relating to fixed assets are capital receipts. Ex. Amount received on the Sale of Machinery, Building, Furniture etc.	2.	Sale proceeds relating to floating or current assets are revenue receipts. Ex. Sale proceeds of stock-in-trade or goods
3.	Any compensation received by a person for the termination of source of his regular income is capital receipt. Ex. Compensation received by an employee from employer for the termination of his services	3.	Any additional income earned by a person in addition to his regular Income is a revenue receipt. Ex. A Gift or reward received by an employee for his good services.

4.	Any compensation received by a person for the surrender of certain rights under an agreement is capital receipt.	4.	Any compensation received by a person under the agreement for the loss of his future profits is revenue receipt.
5.	Any compensation received for the destruction of fixed assets is a capital receipt. Ex. Compensation received from the insurance company for the damage of a machinery due to fire accident.	5.	Any compensation received for the destruction of floating assets is a revenue receipt. Ex. Compensation received from the insurance company for the damage of stock.
6.	If a person keeps an asset as fixed asset in his business, any profit made on its sale is a capital receipt. Ex. If a profit earned on the sale of furniture by the cloth merchant is a capital receipt.	6.	If a person keeps an asset as floating asset in his business any profit made on Its sale is a revenue receipt. Ex. Profit earned on the sale of clothes by a cloth merchant is a revenue receipt.
7.	Compensation received for the cancellation of export licence is a capital receipt.	7.	Amount received for the Transfer of permit or licence is Revenue receipt.

EXAMPLES OF CAPITAL RECEIPTS

1. Compensation received for the surrender of certain rights.
2. Sale proceeds of fixed assets. Ex. Land, Buildings, Machinery etc.
3. Compensation received for the cancellation of export licence.
4. Compensation received from the Transport authorities such as RTC Railways for the permanent disablement.
5. Amount received for the sale of Technical know-how.
6. Compensation received for the illegal removal from employment.
7. Insurance claim received from a Insurance company relating to a fixed asset.
8. Sale proceeds of Trees along with roots.
9. Compensation received from the Govt. for nationalisation of a business.
10. Amount received by the issue of shares.
11. Amount received by the issue of debentures.
12. Any grant or subsidy received for specific purpose.
13. Profits accrued due to variations in the rate of foreign exchange.

EXAMPLES OF REVENUE RECEIPTS

1. Cash discount received by a firm from its creditor for early payment of cash.
2. Compensation received for temporary disablement.
3. Insurance claim received in respect of floating assets.

4. Compensation received for the loss of future profits.
5. Any advance received from the Tenant by the owner.
6. Amount received for the transfer of a permit.
7. Compensation received for the compulsory acquisition of land from the Govt.
8. Rent received on buildings.
9. Interest received on debentures of a company.
10. Sale proceeds of stock or goods.
11. Entertainment Tax collected by a cinema theatre.
12. Pension received by a retired employee.

CAPITAL EXPENDITURE

Expenditure is of two kinds.

EXPENDITURE

Capital Expenditure | Revenue Expenditure

Capital Expenditure

Expenditure incurred on the purchase of fixed assets is known as capital expenditure. In other words if the benefit of an expenditure spreads more than one accounting period it is treated as capital expenditure.

Ex.
1) Amount spent on the purchase of Land & Buildings.
2) Amount spent on the purchase of Furniture and Machinery.
3) Installation expenses of fixed assets.
4) Amount spent on Research and Development etc.

Under the Income Tax Act, 1961 capital expenditure is not allowed to be deducted while computing the total income of a Business or profession.

Revenue Expenditure

The usual and regular expenditure incurred to run a business or an organisation is called Revenue Expenditure. In other words, if the benefit of an expenditure is limited to one accounting period, such expenditure is considered as Revenue Expenditure.

Ex.
1) Salaries paid to the staff.
2) Wages paid to the labourers.
3) Rent paid for the Building.
4) Cost of goods purchased.
5) Renewal fee of Licence etc.

Under the Act, unlike capital expenditure, Revenue Expenditure is allowed to be deducted while computing the total income of a business or profession.

Therefore it is essential to know the differences between capital and Revenue expenditure.

The differences between capital and Revenue expenditure.

Sl.No.	Capital Expenditure	Revenue Expenditure
1)	An expenditure of casual and non-recurring nature is capital expenditure. Eg. Purchase of furniture, buildings, machinery etc.	An expenditure of regular and recurring nature is revenue expenditure. Eg. Rent, Wages, Salaries etc.
2)	An expenditure incurred on the purchase of fixed assets is a capital expenditure. Eg. Cost of Machinery, Furniture, Buildings, Motor, Van etc.	An expenditure incurred on the purchase of floating assets is revenue expenditure. Eg. Cost of goods purchased.
3)	The benefit of capital expenditure spreads for more than one year.	The benefit of revenue expenditure Is limited to one year only.
4)	An amount spent for acquiring the source of income is a capital expenditure.	An amount spent for earning income is revenue expenditure. Eg. Salaries to the staff, wages to the Labourers, Rent for the Building etc.
5)	An expenditure incurred for increasing the earning capacity of a business is capital expenditure. Eg. Expenditure incurred on the Installation of additional seats in a Cinema hall, to meet the demand.	An expenditure incurred for maintaining a fixed asset in working condition is a revenue expenditure. Eg. Cost of repairs to a machinery.
6)	Generally an expenditure pertaining to a fixed asset is a capital expenditure.	Generally an expenditure pertaining to stock-in-trade is a revenue expenditure.
7)	If the object of purchase is not to re-sale the expenditure is a capital expenditure. Eg. Cost of Machine, furniture etc.	If the object of purchase is to re-sale the expenditure is a revenue expenditure. Eg. Cost of Television purchased by dealer.

Examples of Capital Expenditure

1. Cost of acquisition of fixed assets.
2. Installation expenses of fixed assets.
3. Expenses incurred on Research and Development.
4. Registration charges of a land.
5. Consideration paid for the use of Technical know-how.
6. Amount spent for obtaining a licence to start a business.

7. Amount paid to acquire patent rights.
8. Commission paid to an agent for the purchase of a machinery.
9. Commission paid to a broker for raising capital.
10. Amount spent for increasing the earning capacity of an asset.

Examples of Revenue Expenditure

1. Salaries paid to employees.
2. Wages paid to Labourers.
3. Rent paid for the building.
4. Telephone charges.
5. Maintenance charges of fixed assets.
6. Renewal fees of licences.
7. Cost of raw-materials purchased.
8. Cost of goods purchased.
9. Cost of furniture purchased by a furniture dealer.
10. Commission paid to a broker for raising capital.
11. Payment of pension to retired employees.
12. Bad debts.

SUMMARY

INCOME

- Income is very important to a person, a Business organisation and also to the Government for every activity.
- Government gets the income by imposing various taxes. And one among them and the main source of income is through Income Tax.
- Income play a predominant role in the society.

INCOME MEANING AND DEFINITION

- In general, the income means, “Any monetary gain either in the form of money or money’s worth coming from a certain source with some sort of regularity.
- In other sense, the income means the Return on Investment (ROI).
- In Oxford Dictionary, income means; “periodical receipts from one’s business, land, work, investments, etc.
- There are some important features of Income in exist.
- Income Tax Act, 1961, section 2(24) defines about the term income. “It does not give its definitions but widens the scope of the term “income”.
- According to the privy council, an Commissioner of Income-Tax, “income” cannotes a periodical monetary return coming in with some sort of regularity or expected regularity from definite sources which need not be continuously productive, but, their object must be the production of a definite return as distinguished from a mere wind fall.

GROSS TOTAL INCOME

- All incomes shall be classified under the following heads of income.
  - i. Income from salaries.
  - ii. Income from House property.
  - iii. Profits and Gains of Business or Profession.
  - iv. Capital Gains.
  - v. Income from other sources.
- First of all, we have to compute the total income of an Assessee under Head-wise separately.
- Under each head certain deductions have to be made from the Gross income of that head as per the Income Tax rules which come into force from time to time.
  1. After computing the head-wise income separately, these incomes should be added together to find out the Gross total income of an Assessee.
  2. Gross Total income = Income from Salaries + Income from House property + Income from profits and gains of business or profession + Income from capital gains + Income from other sources + Income of other persons to be included in Assessee income.

TOTAL INCOME

- Section 14 of the Income-Tax Act, 1961 deals with the total income of an Assessee.
- In order to derive the total income of an Assessee the following steps are to be followed.
  - vi) Head-wise income should be computed.
  - vii) Admissible head-wise deductions are to be considered.
  - viii) Add together all the Head-wise incomes to get Gross Total income.
  - ix) From the gross total Income certain deductions are to be allowed under section 80D to 80U.
  - x) The Net-amount, thus arrived, is a total income of an Assessee.
- It should be rounded off to the nearest multiple of Rs.10/-.

TAXABLE INCOME

- In order to derive the taxable income of an Assessee, the following steps are to be followed.
  - i) Head-wise income should be computed.
  - ii) Admissable Head-wise deductions are to be allowed.
  - iii) Allow the deductions under section 10.
  - iv) Add together all the Head-wise incomes to get Gross total income.
  - v) From the Gross total income certain deductions are to be allowed under section 80D to 80U.
  - vi) The Net-amount, thus, arrived, is a taxable income of an Assessee.
- The total income of an Assessee will become as an Taxable income of an Assessee.

CASUAL INCOME

- Casual income is that income, the receipt of which is accidental and without any stipulations.

- It is in the nature of unexpected wind fall.

- Under section 10(3), casual income includes

  (i) The winning from lotteries, card games, horse rates etc. to the extent such receipts do not exceed Rs. 5,000/- in the aggregate are called casual income.
  (ii) In the case of winnings from horse races upto Rs.2,500/- in the aggregate only will be treated as casual income.

- Casual income does not include certain voluntary payments like

  (i) Tips given to hotel bearer.
  (ii) Voluntary gift by the parent to a child etc.

CAPITAL AND REVENUE INCOME, EXPENDIURE

- Income Tax is a Tax on income but all incomes are not taxable.
- Revenue receipts are taxable but capital receipts are not taxable.
- Tax liability of an individual depends on the nature of receipt.
- No clear distinction between capital and Revenue items in the Act.
- The judgements or decrees of the various courts are adopted to know the differences.
- Receipts of casual and non-recurring nature are called capital receipts.
- Receipts of regular and recurring nature are called Revenue Receipts.
- Revenue expenditure is allowed to be deducted while computing the income of a business or profession.
- Capital expenditure is disallowed to be deducted while computing the total income.
- Expenditure of casual and non-recurring nature is called capital expenditure.
- Expenditure of regular and recurring nature is called Revenue expenditure.

QUESTIONS

Short Questions

1. What is income ?
2. What are the important features of income ?
3. What is meant by an income according to privy council ?
4. How many heads of incomes are there?
5. How we compute the Gross Total Income (GTI) of an Assessee ?
6. How we compute the Total income of an Assessee ?
7. To which nearest multiple, the total income of an Assessee should be rounded off ?
8. What is Taxable Income ?
9. The Gross Total Income is also to be known as which income ?
10. What is meant by Casual income ?
11. Give any two examples of Casual income ?
12. Give any two examples which cannot be treated as casual income ?

13. Define capital expenditure ?
14. Give four examples of capital expenditure ?
15. What is a revenue expenditure ?
16. Give four examples of revenue expenditure.
17. Write any two differences between capital and Revenue expenditure.
18. Define capital loss. Give two examples of it.
19. What is Revenue loss. Give two examples of it.
20. Why should we know the differences between revenue items and capital items ?
21. What is capital expenditure ? Give an example.
22. Give four examples of capital expenditure ?

Essay Questions

1. Define the income under Income Tax Act, 1961, section 2(24), and explain the scope of the term "income" ?
2. Explain in detail how to compute the Gross Total Income of an Assessee ?
3. Explain in detail how to compute the total taxable income of an Assessee ?
4. Explain the term "Casual income" with suitable illustrations ?
5. Distinguish between capital receipts and revenue receipts with suitable examples.
6. Explain the differences between Revenue Expenditure and capital expenditure with suitable illustrations.
7. Why is it necessary to differentiate between capital losses and revenue losses ? How would you decide whether a particular loss is a capital loss or revenue loss? Explain.

<u>PROBLEMS / PRACTICALS / ILLUSTRATION.</u>

I. Determine whether the following receipts are capital or Revenue receipts with suitable reasons.

1. Compensation received from the Govt. for Nationalisation.
2. Interest on investments.
3. Dividends on shares.
4. Sales tax collected from the buyer of goods.
5. Sale proceeds of furniture.
6. Sale proceeds of furniture by a furniture dealer.
7. Sale proceeds of stock-in-trade.
8. Sale of old news papers.
9. Interest on debentures of Nizam Sugars Ltd.
10. Sale proceeds of building by an estate dealer.
11. Compensation Rs.10,000 received for the cancellation of export licence.
12. Rs.2,000/- received from Ramu for the transfer of permit.
13. Compensation received by General Manager for his illegal removal from employment.
14. Insurance claim received for the loss of machinery in a fire accident.
15. Rs.20,000 received from R.T.C. towards compensation for the permanent disablement.
16. An advance of Rs.5,000 received from the tenant by the owner for letting of his house.

17. Mr. X dealer of Machinery sold a machine to y for Rs.1,50,000 and received the amount in lumpsum.
18. Mr. A dealer of furniture sold furniture to B for Rs.20,000 and he has received the amount in installments.
19. Mr. Rafi an Accounts Officer of IDPL received his salary out of the capital of the company.
20. Mr. Thukaram an author received Rs.6,000/- towards compensation for the surrender of publishing rights.
21. Income Rs.10,000 accrued due to fluctuations in the rate of foreign currency.
22. Mr. Ranjith Singh, Managing Director of SAIL received an amount of Rs.2,00,000 towards compensation for not carrying on competitive business similar to that of the company after retirement.
23. A railway passenger received a compensation of Rs.5,000/- from the Railways for temporary disablement.
24. A colliery owner contracted to supply a certain quantity of coal for 5 years. But the customer after sometime made a breach of contract and did not want to buy coal from the company. Company received an amount of Rs.25,000 from the customer as compensation for the loss of future profits.
25. Lease amount received from the lessee by the lessor under an agreement.
26. Rs.1,000 received towards hire charges of furniture.
27. An amount of Rs.40,000/- received by the issue of shares.
28. An amount of Rs.50,000/- received by HAL by the issue of debentures.
29. Bonus shares received by an investor in a Reliance company.
30. Rs. 1,00,000 received as donation towards building fund.
31. Rs.30,000 received as grant from the State Government.
32. Premium collected on the issue of shares.
33. Mr. E. Raghunadha Rao received Rs.80,000 from Accountant General Office for his retrenchment.
34. Sale proceeds of Radios by a Radio dealers ?
35. Mr. Nancy received Rs.500/- for selling his tape recorder to his friend Shashi.
36. Money received by issue of shares.
37. Sale of Maruthi car by Mr. Satya Sai, a dealer of Bharat motors.
38. Mr. Rama rao received Rs.20,000/- by selling an old machinery.
39. Mr. Jai Rao a stock broker received Rs.2,000/- by selling shares.
40. The Manager received a cash award of Rs.2,000/- from the employer in appreciation of his good services.
41. M. Sunil an outgoing partner received Rs.10,000 from the firm on the condition that he would not run a competitive business for five years.
42. Mr. Rao get a ceiling agency of Bush television from a company for 5 years for Khammam. After 2 years the company directed to make direct selling in Khammam and therefore terminated the company rights of Mr. Rao and the compay paid him Rs.10,000/- as compensation.
43. Mr.B.Nageshwar Rao, owned a petrol pump at Sangareddy. But subsequently the Municipal authorities required the land where the pump has situated and paid him Rs. 80,000 as compenstion.
44. Mr. X while travelling in a Aeroplane, meets with an accident and is temporarily disabled. The Indian Airlines paid him Rs.50,000/- as compensation in lump sum.
45. Salary received by a stenographer in a firm.

46. Mr. Vinod a Sales Manager in Agro-Chemicals Ltd. Received a consideration of Rs.10,000/- for the Termination of his services.
47. Mr.Ramana working as Signal Inspector in Indian Railways received a years bonus of Rs.4,500/-
48. Sale proceeds of old and outdated bags.
49. Sale proceeds of trees along with roots.
50. Mr. Noor received Rs.50,000 on sale of his own building.

ANSWERS :

1. Capital Receipt.
   Reason: It is a compensation for the loss of source of income.
2. Revenue Receipt
3. Revenue Receipt
4. Revenue Receipt
5. Capital Receipt
   Reason: It is a receipt for the sale of a fixed asset.
6. Revenue Receipt.
   Reason: For the furniture dealer furniture is a stock not a fixed asset.
7. Revenue Receipt.
   Reason: Receipt is relating to stock-in-trade.
8. Revenue Receipt
9. Revenue Receipt
10. Revenue Receipt
    Reason: For the Estate dealer building is not a fixed asset.
    It is treated as floating asset.
11. Capital Receipt
    Reason: it is a receipt for the substitute of source of income.
12. Revenue Receipt
13. Capital Receipt
    Reason: It is a compensation for the loss of source of income.
14. Capital Receipt
    Reason: Receipt is relating to a fixed asset.
15. Capital Receipt
16. Revenue Receipt
17. Revenue Receipt
    Reason: For the machine dealer machine is not a fixed asset. It is treated as a stock for him.
18. Revenue Receipt
19. Revenue Receipt
    Reason: It is a revenue receipt for the receiver eventhough it is a capital Payment for the payer.
20. Capital Receipt
    Reason: It is a receipt for the surrender of certain rights.
21. Capital Receipt
22. Capital Receipt
    Reason: It is a compensation for the loss of future profits.
23. Revenue Receipt
    Reason: It is a receipt for the temporary disablement.

24. Revenue Receipt
Reason: It is a compensation for the loss of future profits.
25. Capital Receipt
26. Revenue Receipt
Reason: Hire charges relating to fixed assets are capital receipts.
27. Capital Receipt
Reason: It is a receipt towards the capital of the company.
28. Capital Receipt
29. Capital Receipt
30. Capital Receipt
Reason: It is a receipt for specific pupose.
31. Revenue Receipt
32. Capital Receipt
33. Capital Receipt
Reason: It is a compensation for the loss of source of income.
34. Revenue Receipt
Reason: Radios are treated as goods for the dealer of Radios
35. Capital Receipt
Reason: Receipt is relating to a fixed asset.
36. Capital Receipt
37. Revenue Receipt
Reason: Car is not a fixed asset for the car dealer.
38. Capital Receipt
39. Revenue Receipt
Reason: Shares are treated as stock for the stock broker.
40. Revenue Receipt
Reason: It is a receipt in addition to his regular source of income.
41. Capital Receipt
Reason: It is a compensation for the loss of rights.
42. Capital Receipt
43. Capital Receipt
Reason: Amount is relating to a fixed asset i.e. land
44. Revenue Receipt
45. Revenue Receipt
Reason: It is a regular source of income.
46. Capital Receipt
47. Revenue Receipt
48. Revenue Receipt
49. Capital Receipt
50. Capital Receipt
Reason: Receipt is relating to a fixed asset i.e. building

<u>PROBLEMS / PRACTICALS</u>

V. State whether the following are Revenue or Capital expenses.

1. Mr. Prasad purchased shares of a limited company for Rs.10,000
2. Commission paid to an aged for the purchase of a machinery.

3. Amount spent on the purchase of medicines by a medical shop owner.
4. Air conditioning charges of a building.
5. Cost of goods bought.
6. Money paid to require patent rights.
7. Cost of doors and windows fitted to the building.
8. Commission paid to a broker for raising a loan.
9. Bribe paid to a commercial Tax Officer for evading sales tax.
10. Payment of bonus to employees.
11. Honorarium paid to a Technician for erection of a Machinery.
12. Rs.20,000 spent on the purchase of furniture.
13. Money paid to acquire a license.
14. Cost of repairs made to a building.
15. Salaries paid to staff.
16. Mr. A is the owner of a cinema hall. He has spent an amount of Rs.50,000 for the installation of additional seats.
17. Insurance premium paid in relation to stock-in-trade.
18. A Moon Company Ltd., purchased a Computer and installed it in its office and as a result of this it has retrenched 5 Junior Assistants. An amount of Rs.1,00,000 was paid to them for termination of their services.
19. Cost of raw materials purchased.
20. Mr. Noor incurred an amount of Rs.60,000 for renovation of the building.
21. Mr. Rao purchased an old car and spent Rs.20,000 for its repairs
22. Compensation paid for the termination of contract for the purchase of furniture.
23. Rs.25,000/- incurred to impart training to the employees in the field of the business.
24. Rs.4,000/- paid to an advocate to oppose the Nationalisation of the company.
25. Dashara Pooja expenses.
26. Rs.2,000/- paid to Mr.Rao a clerk for the month of December.
27. Consideration paid to Govt. to take Transport license.
28. Commission paid to a broker to acquire a contract.
29. Goods sold to A proven bad.
30. Salary paid to a clerk out of capital
31. Amount spent on the preparation of partnership Deed.
32. Employers contribution to employees provident fund
33. Legal expenses paid to an advocate to file a suit in the court to protect the assets of a business.
34. Mr. Anil an automobile dealer spent Rs.25,000 towards reconditioning of the purchased lorry.
35. Annual depreciation of a Machinery
36. Mr. Kiran a partner of a firm spent Rs.18,000 for the purchase of a Share of another partner
37. Rs.1,000/- paid towards the registration of a purchased land.
38. Mr. Raju spent Rs.65,000/- for the remodeling of his house.
39. Expenses paid to Eenadu Daily news paper for an advertisement to offer sales at discount.
40. Bribe given to a Bank Manager for raising a loan.

ANSWERS :

1. Capital Expenditure
   Reason: Expenditure is incurred on fixed assets.
2. Capital Expenditure
3. Revenue Expenditure
   Reason: For the dealer of medicines. Medicines are considered as Goods. So any amount spent on purchasing the goods is a Revenue Expenditure.
4. Capital Expenditure
5. Revenue Expenditure
6. Capital Expenditure
   Reason: Amount is spent to acquire the source of income.
7. Capital Expenditure
8. Revenue Expenditure
9. Revenue Expenditure
10. Revenue Expenditure
11. Capital Expenditure
    Reason: Installation expenses of fixed assets are considered as capital expenditure.
12. Capital Expenditure
    Reason: Amount is spent to acquire the fixed asset.
13. Capital Expenditure
    Reason: Amount is paid to acquire the source of income.
14. Revenue Expenditure
    Reason: Maintenance charges of fixed assets are treated as Revenue Expenditure
15. Revenue Expenditure
16. Capital Expenditure
    Reason: Amount is spent for increasing the earning capacity of the business.
17. Revenue Expenditure
    Reason: Amount that relates to a stock-in-trade.
18. Revenue Expenditure
19. Revenue Expenditure
20. Capital Expenditure
    Reason: Expenditure incurred for renovation is a Capital Expenditure
21. Capital Expenditure
    Reason: If an old asset is purchased any amount spent for its repairs is a Capital Expenditure
22. Capital Expenditure
    Reason: Expenditure relates to fixed asset.
23. Revenue Expenditure
    Reason: It is a usual expenditure of a business.
24. Revenue Expenditure
25. Revenue Expenditure
26. Revenue Expenditure
27. Capital Expenditure

28. Revenue Expenditure
29. Revenue Expenditure
30. Revenue Expenditure
    Reason: Salary is a usual and regular expenditure. Hence it is a Revenue Expenditure even though it is paid out of capital.
31. Capital Expenditure
    Reason: Preliminary expenses i.e. expenses incurred for the formation of a business is treated as a Capital Expenditure.
32. Revenue Expenditure
33. Revenue Expenditure
34. Capital Expenditure
35. Revenue Expenditure
36. Capital Expenditure
37. Capital Expenditure
38. Capital Expenditure
39. Revenue Expenditure
40. Revenue Expenditure

5. RESIDENTIAL STATUS

Section 5 of the Act, says that the tax liability of an assessee depends upon his residential status during the previous year. Therefore, the important objective of determining residential status of an assessee is to find out on which of his income the tax may be imposed. For instance, a Resident has to pay tax on all his income whether earned in India or elsewhere, whether received in India or elsewhere. But a non-resident need not pay tax on his foreign income and not ordinarily resident has to pay tax on Indian income and on profits earned profits from a business controlled from India.

The tax liability of each person is based upon his residential status. Section 6 of the Act divides the assessable person in to three categories.
(i) Resident (ii) Resident but not ordinarily resident (iii) Non Resident

Hence we must know whether a person is a Resident or not ordinarily Resident or non-resident during the previous year.

Points to be observed in the determination of residential status :

1. Residential status of an Assessee is decided separately for every year. An assessee who is a resident for one year may be a non-resident or a not ordinarily resident for the other year.
2. The residential status of an assessee changes with his stay in India. For example, Mr. Ansari is leaving India and comes back now and then and because of his frequent movements, his residential status is bound to change.
3. Citizenship of a person should not be taken into account for determining the residential status of a person.
4. For deciding the residential status of a person provisions or conditions stated in the Income Tax Act, 1961 should be taken into account.

The determination of Residential status for the following persons.

1) Individual
2) Hindu undivided family
3) Firm or Association of persons
4) Companies

RESIDENT

AN INDIVIDUAL :

Residence of an individual is classified into three kinds as follows :

1. Resident and ordinarily Resident
2. Resident but not ordinarily Resident
3. Non-Resident

An individual will be treated s Resident if he satisfies any one of the following basic conditions.

Basic Conditions

1. He has been in India for a period of 182 days or more during the previous year
   Explanation :
   i) It is not necessary that the person has been in India continuously for 182 days during such year.
   ii) It is also not necessary that he has been in India at one place i.e. he can stay in his own house or in a hotel or in any other dwelling house.

2. He has been in India for a period of 60 days or more during the previous year and 365 days or more during the four years proceeding the previous year.

Illustration - 1:

Mr.Ansari a foreigner came to India on 25th April, f1999 and never left India. Determine his residential status.

Solution :

For the Assessment year 2000-2001 the relevant previous year is 1999-2000. During the previous year his stay in India was more than 182 days. Hence he is considered as Resident.

Illustration - 2 :

Mr. Samuel an American came to India on 31.12.98 and left India on 31.03.99.

Solution :

Fgor the assessment year 1999-2000 the previous year is 1998-99. During the previous year his stay in India was more than 60 days but he did not stay 365 days during the four years preceeding the previous year. Hence he is not a resident

A resident is classified into two categories as follows :

1. Resident and ordinarily Resident.
2. Resident but not ordinarily Resident.

A Resident will be treated as Resident and ordinarily Resident if he satisfies the following two additional conditions in addition to one of the basic conditions mentioned earlier.

Additional Conditions :

1. He has been resident in India for a 9 years out of 10 years proceeding the previous year.
2. He has been in India for a period of 730 days or more during the 7 years preceding the previous year.

RESIDENT BUT NOT ORDINARILY RESIDENT

A Resident will be treated as Resident but not Ordinarily Resident if he does not satisfy any one or none of the Additional conditions mentioned above.

Illustration:

Mr. John a citizen of America came to India on 5th April, 1999 and left India on 1st January, 2000. Determine his residential during the previous year 1999-2000.

SOLUTION :

For the assessment year 1999-2000 the previous year is 1999-2000. During the previous year Mr. John stayed in India for more than 182 days. It means that he has satisfied one of the primary conditions i.e. presence of 182 days during the previous year. But he has not satisfied any of the additional conditions i.e. presence of 9 years out of 10 years preceeding the previous year and presence of 730 days or more during the seven years preceeding the previous year.

Hence Mr. John will be considered as resident but not ordinarily Resident.

NON-RESIDENT

An individual will be considered as non-resident if he does not satisfy any one of the basic conditions stated earlier.

Illustration :

Mr. P. John an Australian came to India for the first time on 25th April 1997 and left India on 1st September, 1999. Determine his residential status for the Assessment year 2000-2001.

Solution :

For the Assessment year 1995-96 the previous year is 1994-95. During the previous year he has stayed in India for 128 days only. He has not satisfied the first basic condition i.e. presence of 182 days or more during the previous year. According to second basic condition though he has stayed for 60 days during the previous year, he has not stayed even for a single day during the four years preceeding the previous year.

Hence he will be declared as Non-Resident for the Assessment year 2000-2001

A HINDU UNDIVIDED FAMILY (HUF)

Resident

The Manager of a HUF is known "Karta" or head of the family. The other members in the family are known as co-parceners. The "Karta" of the family is liable to pay tax on its income. In the absence of the karta one of the co-parceners will be treated as a manager and he will be liable to pay the tax.

The Residential status of a HUF is as follows :

1) Resident and Ordinarily Resident
2) Resident but not ordinarily Resident
3) Non-Resident

RESIDENT

A HUF will be considered as Resident if it satisfies the following basic condition.

Basic Condition :

The control and management of the affairs of a HUF either wholly or partly situated in India during the previous year.

The control and management of affairs means the decision making power of vital decisions.

Eg.
1) Decisions relating to nature of Business.
2) Appointment of staff
3) Fixation of salary structure etc.,

Illustration-1 :

A HUF located in Hyderabad is managed by Mr. Varma. During the previous year 1999-2000 he was in India – Determine the residential status of HUF.

Solution :

During the previous year 1999-2000 the Karta was in India. It means that the control and management of its affairs are wholly situated within India. Hence HUF is considered as a resident.

Illustration-2 :

Mr. Raju is a Karta of a HUF. During the previous year 1999-2000 he was in Japan and took all the important decisions of HUF there only.

Solution :

For the assessment year 1991-92 the previous year is 1990-1991. During the previous year 1990-91 he was not in India. He did not delegate any of his powers to any of the other members of the family and he took all the decisions outside India. It means that the control and management of a HUF are wholly situated outside India. Hence HUF is not a resident during the previous year.

RESIDENT AND ORDINARILY RESIDENT

If Karta or Manager of HUF satisfies the following two conditions in addition to the above said basic condition its residential status will be declared as Resident and ordinarily resident.

Additional Conditions :

The karta or the manager of a HUF has been in India as resident for 9 years out of 10 years preceding the previous year.

The karta or the manager of a HUF has been in India for a period of 730 days or more during the 7 years preceding the previous year.

RESIDENT BUT NOT ORDINARILY RESIDENT

A Resident HUF will be declared as Resident but not ordinarily Resident if karta does not satisfy one or none of the above stated additional conditions.

Illustration-I :

Mr.Amar the 'Karta' of a HUF located in Tamil Naidu has been residing there since 1976 . He never left India at any time. Determine its residential status during the previous year.

Solution :

During the previous year the residential status of the HUF will be considered as not ordinarily resident i.e., resident but not ordinarily resident because the karta has satisfied the basic condition i.e. the place of control and management should be in India and both the additional conditions i.e. presence of 9 years out of 10 years preceeding the previous year and presence of 730 days or more during the 7 years preceeding the previous year.

NON-RESIDENT

A HINDU UNDIVIDED FAMILY

A HUF will be considered as a Non-Resident if the control and management of its affairs are situated wholly outside India.

Illustration :

Mr. Sheshavataram is a 'Karta' of a HUF, situated in the West Godavari District. During the previous year he was in America. In his absence no other member has been appointed to look after its affairs.

It means that the control and management of its affairs are situated wholly outside India. Hence its residential status is Non-resident.

RESIDENT

A FIRM

Under section 6(2) of the Income Tax Act a firm is said to be resident during the previous year if the control and management of the firm are partly or wholly situated in India during the previous year.

Illustration-1 :

A,B,C are the partners of a partnership organisation. During the previous year they assembled in a Lakshmi Lodge at Hyderabad and discussed all the important matters of their business. Determine its residential status.

Solution :

During the previous year all the partners were in India and took all the important decisions in India. It means that the control and management of the firm are wholly situated within India. Hence the firm will be treated as Resident during the previous year.

Illustration-2 :

Mr. Shafi an Indian and Mr. Saimual an American together opened a Medical shop in Madras. But as per their agreement they have to meet once in six months in China to review their business. Determine the residential status of the firm.

Solution :

For determining the residential status of a firm the place of control and management are taken into account. But in this case they are meeting outside to take the vital decision relating to their business. It means that the control and management of the firms are wholly situated outside India. Hence it is not a resident during the previous year.

NON-RESIDENT

A FIRM

A firm is said to be a non-resident in India where the control and management of its affairs are situated wholly outside India during the previous year.

Illustration :

Mr. Keerthi Kumar owner of Cloth Business located at Sangareddy. During the previous 1994-95 he was in Japan on a business tour and took all the important decision pertaining to the business in Japan and he communicated such decisions to his employees in India. Determine the residential status of the firm ?

Solution :

To decide the residential status of a firm, the place of control and management is taken into account. During the previous year the owner of the business was out of India and took all the decisions outside India. It means that the control and management of its affairs are situated wholly outside India. Hence the firm will be treated as non-resident for tax purpose.

AN ASSOCIATION OF PERSONS

RESIDENT

An Association of persons means a union of persons established to achieve a specific object.

Ex. 1) A chamber of commerce
2) A club
3) A co-operative society

An association of persons said to be resident where the control and management of its affairs are partly or wholly situated in India during the previous year.

AN ASSOCIATION OF PERSONS

NON-RESIDENT

An Association of Persons or a union of persons is said to be Non-Resident, where the control and management of its affairs are situated wholly outside India during the previous year.

A COMPANY

RESIDENT

Under Income Tax Act a company may be resident or Non-resident. A company is treated as resident if any one of the following two conditions are satisfied.

i. If the Company is an Indian company. A company is said tobe Indian company if it is incorporated or registered under the Indian companies Act, 1956 or any other Act which was in force.
ii. If the Control and Management of its affairs are wholly situated in India.

Ex. Lakshmi Electricals company producing Electrical goods is located in Hyderabad. The Board of Directors of the company are meeting once in three months at Banjara Hotel in Hyderabad to review the operations of the company, determine its residential status during the previous year.

Solution :

The place of control and management of a company are taken into account for deciding the residential status of a company. Control and management means the place where the Board of Directors meet. In this case the meetings of the Board of Directors are held within India. It means that the Control and Management of this company is within India. Hence its residential is treated as resident.

NON-RESIDENT

A company is treated as a non-resident.

1. If it is not an Indian company
2. If the control and management of its affairs are situated wholly outside India.

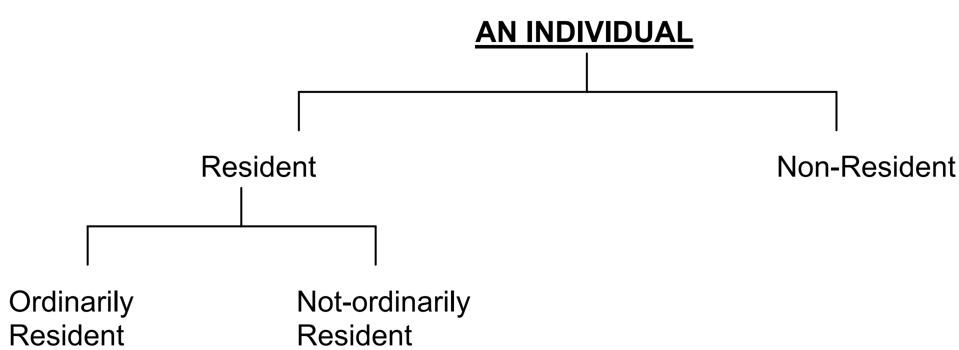
Illustration :

A Foreign based Pepsi Company is established in India to supply Cool drinks to Indians. Determine its residential status ?

Solution :

The residential status of the company is non-resident as the company is not incorporated or registered under the Indian Companies Act.

RESIDENTIAL STATUS OF DIFFERENT ASSESSES



A HINDU UNDIVIDED FAMILY

- Resident
  - Ordinarily Resident
  - Not-ordinarily Resident
- Non-Resident

AN ASSOCIATION OF PERSONS

- Resident
- Non-Resident

A FIRM

- Resident
- Non-Resident

A COMPANY

- Resident
- Non-Resident

EASY TO REMEMBER

INDIVIDUAL

Resident: Satisfies one of the Basic conditions.

Non-Resident: Does not satisfy any of the Basic conditions.

Resident and Ordinarily Resident : Satisfies both the additional conditions in addition to one of the basic conditions.

Resident but not Ordinary Resident: Satisfies one of the basic conditions and does not satisfy one or none of the additional conditions.

H.U.F.

Resident : Control and Management fully or partly in India.

Non-Resident: Control and Management fully outside India.

Resident and Ordinary Resident: Kartha satisfies two additional conditions in addition to basic condition.

Resident but not Ordinarily Resident: Kartha does not satisfy one or more of the additional conditions.

A FIRM / AN ASSOCIATION OF PERSONS / COMPANIES

Resident : Control and Management fully or partly in India.

Non-Resident: Control and Management fully outside India.

SUMMARY

- Scope of total income of an assessee depends upon his residential status during the previous year.
- Residential status of an assessee changes with number of days he stayed in India.
- Citizenship should not be taken into account for determining the residential status of an assessee.
- Provisions of Income Tax Act have to be followed for deciding the residential status.
- Section 6 of the Act deal with the various provisions for determining the residented status of different assessees.
- An individual and a HUF may be resident, ordinarily resident, not ordinarily resident and non-resident.
- A firm, a company, an association of persons and every other person may be resident or non-resident only.
- The head of the HUF is known as 'Karta'. The other members of the family are known as co-parceners.
- To decide the residential status of a HUF, a firm, a company, an association of persons and every other person place of control and management are vital factors.
- Control and management means decision making power of important matters.
- A HUF, a firm, a company, an association of persons and every other person is resident if the control and management are situated wholly in India and non-resident if the control and management are situated wholly outside India.
- For deciding the residential status of an individual the conditions laid down in the Act are to be observed.

QUESTIONS

Short Questions

1. What are the different categories of Assessees according to this Residential status ?
2. Who is a non-resident ? (individual) ?
3. Which is a resident firm ?

4. Under what circumstances on HUFmay be considered as resident in India during the previous year ?
5. Which is a non-resident company ?
6. State one reason why residential status of persons is determined ?
7. What is the basic condition to decide the residential status of a Hindu Undivided Family ?
8. What is the basic condition to decide the residential status of a company ?
9. Which is an Indian Company ?

Essay Questions

1. How do you determine the residential status of an individual ?
2. Write short notes on :-
    a) Resident and Ordinarily Resident
    b) Resident but not Ordinarily Resident
    c) Non-Resident
3. How do you determine the residential status of the following ?
    a) A firm
    b) A company
    c) An Association of Persons

Problems/Practicals

1. Mr. Arjun a citizen of India left for Russia for the first time on 20.09.1985 on a business trip. He returned to India on 15.06.1986. What will be his residential status for the assessment year 1987-88. (Ans: Resident)
2. Mr. Omkar went to West Germany for studying MBA on 5^{th} September, 1986 and never came to India. What is his residential status for the year ending on 31^{st} March, 1987. (Ans: Non-Resident).
3. Mr. Dorai a citizen of India left for Bangladesh on 20.06.1994. He returned to India on 20.06.95. But he never resided India in the past. Determine his residential status for the year ending 31^{st} March, 1986. (Ans. Resident but not Ordinarily Resident)
4. Mr. Rafi came to India for the first time on June 10, 1994. He left India on December 20, 1994. What will be his residential status for the assessment year 1995-96. (Ans. Resident).
5. Mr. Laloo an Indian left India on 2^{nd} October, 1990. He returned to India on 2^{nd} March, 1995 and stayed in India upto 31^{st} March, 1995. Determine his residential status for the assessment year 1995-96 (Ans. Non-Residnt).
6. Mr. Dass who is a Karta of a Hindu Undivided Family, resided in Japan during the previous year. What will be the residential status of a HUF during the assessment year ? (Ans. Non-Resident).
7. XYZ company which is not registered under Indian companies Act has been established in India. The Board of Directors of the company is situated at London. Determine the residential status of the company during the assessment year. (Ans. Non-Resident).

INCIDENCE OF TAX

Tax is levied on the total income of assessee.

Scope of the total income of an asessee is dealt under section 5 of the Income Tax Act, 1961.

Tax liability of different persons is determined with reference to their residential status during the previous year.

Under the Act income of a person is divided into two categories, they are :

I) Indian Income
II) Foreign Income

I) INDIAN INCOME

The following incomes are treated as Indian Income.

1. Income accrues or arises or is deemed to accrue or arise to him in India and received in India by or on behalf of such person.

Examples:

a) Dividends received from Indian company.
b) Interest received on deposits.
c) Income from a house property in India.
d) Income earned in America but received in India.

2. Income accrues or arises or is deemed to accrue or arise to him in India but received outside India.

Examples :

a) Rs.10,000 earned in India but received in Bangladesh.
b) Salary received by Indian employees working in other countries.
c) Rs.20,000 is the profit of a business in America, the business controlled from India.

3. Income accrues or arises or is deemed to accrue or arise to the outside India but such income is received in India.

Examples :

a) Rs.10,000 earned in Japan and received in India.
b) Profit from business in America received in India Rs.7,000.
c) Income from house property in Srilanka received in India Rs.5,000.

II) FOREIGN INCOME

Income earned in other countries and received in other countries is called a Foreign income.

Examples:

a) Profit earned from a business in Germany Rs.10,000.
b) Income from a house property in Pakistan Rs.25,000.
c) Income from land situated in Burma Rs.15,000.

Income to be included in the total income of :-

1) Resident and Ordinarily Resident.
2) Resident but not Ordinarily Resident
3) Non-Resident.

1. RESIDENT AND ORDINARILY RESIDENT :

Under section 5(1) of the Act, the resident and ordinarily resident have to pay tax on the Indian income and Foreign Income. Therefore, the total income of the resident and the ordinarily resident includes :-

a) Income accrued or arises or is deemed to accrue or arise to him in India and received in India.
b) Income accrues or arises or is deemed to accrue or arise to him in India but received outside India.
c) Income accrues or arises or is deemed to accrue or arise to him outside India but such income is received in India.
d) Income accrues or arises to him outside India and received outside India.

2. RESIDENT BUT NOT ORDINARILY RESIDENT :

He has to pay tax on Indian Income only. He need not pay any tax on Foreign Income. But there is an exception to this general rule. If an assessee has a business outside India and if the control and management of the business is in India, then the income earned from such business also has to be included in his total income. Therefore the total income of the resident but not ordinarily resident includes :-

a) Income accrues or arises or is deemed to accrue or arise to him in India and received in India.
b) Income accrues or arises or is deemed to accrue or arise to him in India but received outside India.
c) Income accrues or arises or is deemed to accrue or arise to him outside India but such income is received in India.
d) Income accrues or arises to him outside India from a business whose control and management is set up in India.

3. NON-RESIDENT :

If the residential status of an assessee is non-resident he has to pay tax on Indian income only. He need not pay tax on foreign income, even though he has a business outside India but controlled from India. Therefore the total income of Non-resident includes :-

a) Income accrues or arises or is deemed to accrue or arise to him in India and received in India.
b) Income accrues or arises or is deemed to accrue or arise to him in India but received outside India.
c) Income accrues or arises or is deemed to accrue or arise to him outside India but such income is received in India.

RECEIPT OF INCOME

Receipt of Income means that the income received on the first occasion by an assessee. In other words, the place of receipt of income shall be the place where it is received for the first time and not the place of its receipt on subsequent remittance.

Thus an income earned outside India and received outside India (Foreign Income) is not taxable even if it is remitted to India unless it is received or is deemed to be received in India.

Income may be received either in Cash or Cheque or by simple cross entries. Income need not always be received in Cash. Even receipt by an agent or by any person appointed on behalf is enough to attract tax.

ACCRUAL OF INCOME

Accrual of income means that the income earned but has not been actually received but it is deemed to be received under the Income Tax Act.

Examples :

i) Annual accretion to the Provident Fund Account. Though it is not actually received by the employee, it is deemed to be received by him under the Act;
ii) Company declared dividends but not received by the share holders. Dividends are deemed to be received in the year in which they are declared;
iii) Taxable portion of transferred balance from an un recognised provident fund account to a recognised provident fund account.

INCOME DEEMED TO ACCRUE OR ARISE IN INDIA

Income deemed to accrue or arise in India means that the income has actually not accrued or arisen in India but it is deemed to accrue or arise in India under the Income Tax Act.

Examples :

i) Salary payable by an employer to an employee of India for the services rendered outside India.

ii) Salary earned in India whether received in India or outside India.

iii) Dividends paid by a company outside India are deemed to accrue or arise in India.

iv) Income accrues or arises from any Trade or business in India.

Summary table showing the incomes to be included in the total incomes of different assessees :

Particulars	Residential Status		
	Resident & ordinary Resident	Resident but not Ordinarily Resident	Non-Resident
Income accrues or arises or is deemed to accrue or arise in India and received in India.	Taxable	Taxable	Taxable
Income accrues or arises or is deemed to accrue or arise to him in India but received in outside India.	Taxable	Taxable	Taxable
Income accrues or arises or is deemed to accrue or arise to him outside India but such income is received in India	Taxable	Taxable	Taxable
Income earned outside India and received outside India from a business controlled from India.	Taxable	Taxable	Not-Taxable
Income accrues or arises to him outside India and received outside India.	Taxable	Not Taxable	Not-Taxable
Income earned and received outside India and brought such income to India subsequently.	Not-Taxable	Not-Taxable	Not-Taxable
TOTAL INCOME	xxxxxx	xxxxxx	xxxxxx

SUMMARY

- The scope of the total income of an Assessee is described under section 5 of the Income Tax Act, 1961.
- The tax liability of an Assessee is determined on the basis of his residential status.
- Incomes earned in India and received in India, income earned in India and received outside India and Income earned outside India and received in India are called Indian incomes.
- Income earned and received outside India is a Foreign Income.
- Assessee's total income includes :
  i) Indian Income ii) Foreign Income
- Taxable income of a Resident and ordinarily resident includes
  i) Indian Income and ii) Foreign Income
- Taxable income of a Resident but not ordinarily resident includes
  i) Indian Income
  ii) Business income from outside India which is controlled from India.
- Non-Resident has to pay tax on Indian Income only.
- Receipt of income means the Income received on the first occasion by an assessee.
- Foreign income brought to India subsequently is not taxable.
- Accrual of income means the income earned but has not been actually received but is deemed to be received under the Act.
- Income deemed to accrue or arise in India means the income has actually not accrued or arisen in India but it is deemed to accrue or arise in India under the Act.

I Short Questions

1. What is meant by incidence of Tax ?
2. What is an Indian income ?
3. What is a Foreign Income ?
4. What is income received in India ?
5. Which income deemed to accrue or arise in India ?
6. Give two examples of income which are deemed to be received in India ?
7. Which incomes are to be included in the taxable income of a Resident assessee?
8. Which incomes are to be included in the taxable income of a Resident but not ordinarily resident ?
9. Which incomes are to be included in the taxable income of a Non-Resident ?
10. What do you mean by receipt of income ?

II Essay Questions

1. Distinguish between India income and Forein income with suitable examples.
2. The incidence of Tax depends upon the Residential of an assessee – discuss.
3. Discuss the scope of the taxable income of the following assessees :
   i) Resident and ordinarily resident
   ii) Resident but not ordinarily resident.
   iii) Non-Resident.
4. Explain how the tax liability of an assessee is determined with reference to his residence.

6. EXEMPTED INCOMES

Income Tax is a tax on income, but all incomes are not taxable. Under section 10 of the Income Tax Act, 1961, some incomes are exempted from Tax. In other words some incomes should not be included in the total income of an assessee and some incomes are included in the total income but are exempted from Tax.

Meaning of Exempted Income :

Exempted income is an income on which income tax is not imposed. It is a tax free income and hence assessee need not pay any tax on it.

The exempted incomes are of three kinds :

1. Exempted incomes to individual.
2. Exempted incomes to institutions and Authorities.
3. Exempted income to Non-Residents.

According to revised syllabus, we have to study the exempted incomes concerned to individuals only.

EXEMPTED INCOMES TO INDIVIDUALS

The following income shall not be included in the total income of an individual and are not taxable.

1. Agricultural Income [Section 10]
2. Income received from a HUF(Hindu Undivided Family) [Section 10(2)]
3. Casual or unexpected incomes [Section 10(3)]
4. Travel Concession [Section 10(5)]
5. Perquisites allowed to an individuals working outside India [Section 10(7)]
6. Any income received under co-operative Technical Scheme [Section 10(8 & 9)]
7. Death-cum-retirement gratuity [Section 10(10)]
8. Commuted value of pension [Section 10(10A)]
9. Encashment of leave salary [Section 10(10AA)]
10. Retrenchment compensation paid to workers [Section 10(10B)]
11. Amount received from life insurance policy. [Section 10(10D)]
12. Amount received from statutory provident fund. [Section 10(11)]
13. Amount received from Recognised provident fund. [Section 10(12)]
14. Payment from an approved super annuation fund. [Section 10(13)]
15. House Rent Allowance. [Section 10(13A)]
16. Special Allowance received by an employee for the performance of his duties. [Section 10(14)]
17. Interest received on Tax free securities. [Section 10(15)]
18. Scholarships granted to the students. [Section 10(16)]
19. Daily and other allowances to M.Ps or M.L.As. [Section 10(17)]
20. Ex-gratia payments received from Central Government. [Section 10(18A)]
21. Income received by any member of scheduled tribes. [Section 10(26)]
22. Annual value of any palace occupied by a former ruler. [Section 10(19A)]
23. Income received by an individual from charitable funds. [Section 10(23C)]
24. Subsidy or any other assistance received from Tea Board. [Section 10(30)]
25. Any subsidies received by planters. [Section 10(31)]

1. Agricultural Income [Sec 10(1)]

Under section 10(1) of the Act Agriculture income means any income derived from land which is situated in India and is used for Agriculture purpose.

State Governments are already collecting tax in the form of land Revenue on Agriculture income. Hence it is exempted from Tax. However the concept of Agriculture income is discussed under Sec. 2(1) in detail in the earlier chapter.

2. Income from a H.U.F.[Section 10(5)]

Any amount received by a member or co-parcener from a Hindu undivided family is fully exempted from tax.

3. Casual Income [Section 10(3)]

An income which is unexpected and unforeseen is known as casual income.
Example:

i) Gifts received on birthday functions.
ii) A prize from a lottery.
iii) Money found lying on the road.
iv) Award received for Tracing a lost child.

Under the Act casual income is exempted upto Rs.5,000/- and the balance amount is taxed at the rate of 40%.

Note: Incase of races including horse races exemption is given upto Rs.2,500/- only.

4. Travel Concession [Section 10(5)]

Any travel concession received by an employee being a citizen of India from employer to proceed to any place in India after retirement or during service or after the termination of his services.

5. Allowances or perquisites outside India [Section 10(7)]

Allowance or perquisites allowed by the Indian Govt. to an Indian employee working outside India are exempted from the tax. But this exemption is not given to the following persons.

i) Non-Government Employees
ii) Those who are not citizen of India.

6. Any income received under co-operative Technical Scheme [Section 10(8)]

As per the agreement made between Indian and Foreign Government, for the exchange of co-operation and technical assistance, if any person is assigned duties in India, any income derived in India is exempted from tax. If any income accrues or deemed to accrue outside India and received in India is also exempted from tax.

7. Death-cum-Retirement Gratuity under [Section 10(10)]

Any gratuity received by employees of Central Government, State Government, a local authority, a corporation established by a Central, state or provincial Act is exempted from tax. In case of other employees like employees in the private sector exemption is calculated as shown below.

<u>Assessee</u>

- Government employees etc. the full amount of such gratuity receive.
- Other employee
  - Received gratuity strictly as per the payment of Gratuity Act, 1972 full amount of such gratuity received.
  - If gratuity is received at better terms least of the following is exempted.
    1) Actual amount of Gratuity received.
    2) ½ month salary for each year of completed service i.e. any fraction of the year will be ignored.
    3) Rs.2,50,000/-

8. Commuted value of Pension under section 10(10A)

The total amount of commuted value of pension received by the employees of the Government a local authority or a statutory corporation is exempted from tax.

9. Encashment of leave salary under section 10(10AA)

Any payment received by the employees of Central and State Governments as the cash equivalent of the leave salary in respect of the earned leave at his credit at the time of his retirement shall be fully exempted from tax.

10. Retrenchment compensation paid to workers under section 10(10B)

Any compensation received by a workman under the Industrial Disputes Act, 1947 will be exempted from payment of tax provided the amount is calculated is in accordance with the provisions of the Industrial Disputes Act or Rs.50,000/- whichever is less.

11. Amount received from the Life Insurance Policy under Section 10(10D)

Any payment received under a life insurance policy including bonus will be exempted from tax with retrospective effect from 01.04.1962.

12. Amount received from a statutory provident fund under section 10(11)

Any some received from a statutory provident fund is fully exempted from tax. A statutory provident fund is a fund to which provident fund Act, 1925 applies.

13. Amount received from recognised provident fund under section 10(12)

A recognised provident fund is a fund which is recognised by the Commissioner of Income Tax. Any payment received from such fund is fully exempted from tax.

14. Payment from a approved super annuation fund under section 10(13)

It is a fund which is approved by Commissioner of Income Tax as per the rules specified in Part 'B' of the schedule IV of the Income-Tax Act. Payments from this fund are totally exempted from tax (complained in detail in Salary income)

15. House Rent Allowance under section 10(13A)

If the employer does not provide residential accommodation, some allowance is given to him to meet the cost of residential accommodation. This is known as House Rent Allowance. It is exempted subject to conditions mentioned in the Act.
(EXPLAINED IN DETAIL IN SALARY INCOME)

16. Special Allowance received by an employee for the performance of his duties under section 10(14) :

Any special allowance or benefit specially granted to meet expenses incurred in the performance of the duties will be exempted from tax only to the extent notified by the Central Government.

17. Interest received on Tax free securities under section 10(15)

Interest on the following securities is totally exempted from tax.

a) Treasury savings Deposit certificates.
b) Post Office Cash Certificates.
c) National Plan Certificates.
d) Post Office National Savings Certificates.
e) 12 years National Plan Savings Certificates.
f) 10 years Defence Deposit certificates.
g) The Government of India Defence Certificates.
h) 12 year National Defence Certificates.
i) Interest on securities held by the issue department of the Central Bank of Ceylon.
j) Premium Prize Bonds, 1963.
k) 7 years National Savings Certificates (II issue).
l) 7 years National Savings Certificates (III issue).
m) Bonus on deposits in post office savings bank and interest in respect of deposits under the Post Office Savings Bank (Cumulative Time Deposit) Rules 1959.

n) Interest credited on deposits under the Public Provident Fund Scheme.
o) Interest on Government Savings certificates (Fixed Deposits).
p) Interest on Post Office fixed deposits.
q) Annual payment on National Defence Gold Bonds, 1980.
r) Monthly payment on 15 years annuity certificates issued by the Government.
s) Interest on notified capital investment bonds.
t) Interest on cumulative time deposits (As per CBDT circular No.410, dt: 12.2.85).

18. Scholarships under section 10(16)

Any scholarships granted to the students to meet their cost of education is fully exempted from tax.

19. Daily Allowances to M.Ps and M.L.As under section 10(17)

Daily and other allowances granted to the Members of the Parliament and to the Members of the Legislative Assembly are totally exempted from tax.

20. Ex-gratia payments by the Central Government under section 10(18A)

Any ex-gratia payments made by the Central Government consequent on the abolition of privy purse are fully exempted from tax.

21. Annual value of any palace under section 10(19A)

The annual value of any palace or a building occupied by a former ruler is fully exempted from payment of tax.

22. Income from charitable funds under section 10(23C)

Any income received by an individual from the following funds is exempted from tax.

a) PM National Relief Fund.
b) The Prime Ministers Fund (Promotion of Folk Arts).
c) The P.Ms Aid to Students Fund.

23. Income received by any member of scheduled tribes under section 10(26)

Any income derived by any member of scheduled tribes residing in Nagaland, Manipur, Tripura, Arunachalpradesh and Mijoram is fully exempted from tax.

24. Subsidy or any other assistance received from Tea Board under section 10(30)

Any subsidy received from Tea Board for replantation or replacement of Tea Bushes by an assessee who carries on the business of growing and manufacturing Tea in India is totally exempted from Tax.

25. Any subsidies received from planters under section 10(31)

Any subsidy received by an assessee who is engaged in the business of growing and manufacturing Rubber, Coffee, Cardamom or any other commodities as the Central Government notify from time to time will be exempted from tax from the assessment year 1989-90.

SUMMARY

Exempted incomes are those incomes which are not subject to tax. The assessee need not pay tax on such incomes.

Exempted incomes are classified under three heads i.e.

a) Exempted incomes to individuals
b) Exempted incomes to institutions and Authorities.
c) Exempted incomes to non citizens.

Some incomes are included in the total income but are exempted from tax. They are included in the total income only for the purpose of determining the rate of tax.

Tax free securities means interest received on such securities is fully exempted from tax.

The exempted incomes are dealt with under section 10 of Income Tax Act.

I. Short Questions

1. What is an exempted income ?
2. Mention the kinds of exempted incomes ?
3. Under which section of the Act the exempted incomes are dealt with ?
4. Give two examples of incomes which are totally exempted from the payment of tax ?
5. Write any two examples of incomes which are included in the total income of an assessee but are exempted from the tax ?
6. Give two examples of exempted incomes of an individual ?

II Essay Questions

1. Enumerate any ten incomes which are exempted from the charge of Income Tax?
2. Mention the exempted incomes to non-citizen ?
3. Discuss ten exempted incomes of an Individuals ?

7. INCOME FROM SALARY

An Assessee whether he is a Government employee or a private employee must pay Income Tax if his income from salary exceeds tax exemption limit fixed by the Government.

Heance there is a need to learn the meaning of salary, different kinds of allowances and perquisites, computation of taxable income etc., to determine the amount of tax payable by an employee.

The word 'salary' is defined differently. Any remuneration received by an employee from employer is salary. In simple words, salary means the income of a person which he received from his employer for rendering services to him. But every remuneration received for rendering services by lawyer, medical practitioner will be professional income. It must be noted that income belong to a specific head must be treated top tax under that head only. According to provisions of specific head any expenditure incurred to earn an income should be deducted from the gross income of such head.

Important Features of Salary

1 **Employee and Employer Relationship :** In order to tern any income as income from salary the most important characteristic of salary, is the existence of employee and employer relationship. To be more specific, this relationship should be that of a 'master' and 'servant'. Therefore any fees received by a consultant, director (not being whole time director) cannot be treated as salary. Employer may include Government, local authority, a public body or association, foreign government or others. Payments received from any person, other than employer are nor taxable under this head. If an employee does any work for his employer which is not connected with his service, then the remuneration for such work will be treated as salary e.g..examiner's remuneration received by a teacher from his university shall be treated as income from other sources.

2 **Salary may be paid in cash or in kind :** Salary may be paid either in cash or in kind.

3 **Salary of a Member of Parliament:** The salary of Member of Parliament of government by the 'salaries' and 'allowances' of Members of Parliament Act 1954, Hence it is not chargeable to tax under the head 'salaries'. A member of parliament is not a government employee. The same shall be taxable under the head 'income from other souces'.

4 **Employment and profession:** Employment must be distinguished from profession. If employment is merely the exercise of a profession the gains from such employment are not taxable under the head salaries. For example a chartered accountant may be engaged by a company to audit the accounts of

such company for some remuneration, the remuneration from such engagement shall be taxable as professional income. But, if the same chartered accountant is given employment in the company as the internal auditor, any remuneration so received shall be taxable under the head 'Salaries'.

5 **Remuneration revceived by partner of a firm:** Any salary, commission, bonus fees or any other remuneration received by a partner of a firm, by whatever name called, shall be taxable under the head 'profit and gains' of business or progession'.

6 **Payment received after the discontinuation of service from his former employer is also taxable under the head 'salary'**

7 **Salary from more than one employer:** It makes no difference wherther the employee has received salary from one employer or from more than one employer during a financial year due to change of employment. The aggregate amount of salary received during a particular financial year shall be put to tax under the head 'salaries'. But, If any remuneration is received from two different sources, the remuneration from the employer shall be taxable under the head salaries. Other remuneration shall be taxed under the head income from other sources. e.g. Lecture fees received by a doctor working in a Government hospital is 'income from other sources'

8 **Salary is taxable either on 'due' basis or on ' receipt' basis whichever is earlier.**

9 **Tax-free Salary:** Where and employee received tax-free salary i.e. tax is paid by the employer. Then the employee has to include the amount of tax paid by his employer on his behalf to the net salary received so as to ascertain actual salary for tax purpose.

10 **Voluntary foregoings:** The voluntary foregoings of the salary due to him by an employee shall be treated as application of the income and the same is full taxable.

11 **Surrender of Salary:** Any agreement between employee and employee and employer, that, employer need not pay any salary. Would not attract any tax liability.

12 **Pension:** Pension received by an employee after his retirement is treated fro all practical purposes as salary. Regarding commuted pension, exemption rules are applicable on the basis of nature of employment, which are explained in the later part of the present lesson. Foreign is taxable on the basis of residential status.

13 **Deductions by employer:** Compulsory statutory deductions such as, tax deducted at source, contribution to provident fund, medical and staff welfare scheme etc.. the employer are mere application of income. Hence all these are to be added back to his net salary received to find out salary.

14 **Family pension:** Any pension paid to the widow or legal heir of the deceased employee shall not be treated as 'salary'. Instead the same will be taxed under the 'income from other sources'.

Due dates of salary

A) In the case of government and non government employees:
Normally the salary of a particular month becomes due on the first day of next month. In such a case the current financial year will be 1st April to 1st March of next year.

B) In the case of non- government and bank employees: The salary of each month may become due on the last day of the same month. Current financial year in such case will be April to 31st March of the next year.

Chargeability Sec. 15

Under section 15 of the Income –tax Act 1961 the following incomes shall be taxable under the head 'Salaries'.

i) any salary due from an employer or a former employer to an assessee in the previous year, whether paid or not,
ii) any salary paid or allowed to him in the previous year by an employer or former employer, whether due or not, and
iii) any arrears of salary paid or due to him in the previous year by and employer or a former employer, if not charged to income –tax in any earlier previous year.

Computation of taxable salary

Various items relating to 'salary income' are provided in the Income-tax Act 1961 in the following order.

Section 15 - Chargeability of salary.
Section 16 - Deductions allowed out of salary income.
Section 17 - Perquisites inlcudible in salary.
Section 17 (3) (ii) - Allowances and other items includible in salary.
Section 17 - Profits in lieu of salary.

These provisions will help us in determining income from salary. This can be illustration in the following chart. 99

Salary

Basic salary + Allowances + Perquisites + Profits-in-lieu of salary

Less

Standard deduction + Entertainment Allowance + Employment tax
u/s 16(i) u/s 16(i) u/s16(iii)

Method of computation of salary income.

I.	**Salary**	**Rs.**	**Rs.**
	Basic salary		x x x
	Bonus		x x x
	Commission		x x x
	Fees		x x x
	Overtime – remuneration		x x x
	Leave encashment		x x x
	Employer's contribution to RPF in excess of Prescribed limit		x x x
	Interest credit to RPF In excess of prescribed limit		x x x
II	**Allowances**		
	A. Fully taxable allowances		x x x
	B. Partly taxable allowances	x x x	
	Less: Deductible/exempt	x x x	x x x
	C. Allowances not taxable		N.T
III	**Perquisites**		
	A. Taxable in all cases of employees		x x x
	B. Taxable in specified cases of employees		x x x
	C. Perquisites not taxable		N.T
IV	**Profits in Lieu of Salary**		x x x
	Gross Salary		x x x
V	**Deductions**		
	Less : Deduction u/s 16(i): standard deduction	x x x	
	: Deduction u/s 16(i): entertainment allowance	x x x	
	: Deduction u/s 16(i): employment tax/ Professional tax	x x x	x x x
	INCOME FROM SALARY		x x x
ADD	Income from the other source		x x x
	Gross Total Income		x x x
VI	**DEDUCTIONS**		
	i) 80 D	x x x	
	ii) 80 DD	x x x	
	iii) 80 DDA	x x x	
	iv) 80 E	x x x	
	v) 80 G Etc.	x x x	x x x
	Total Income		x x x

Allowances

All allowances are liable to be included in salary income unless otherwise exempt from tax. Any periodic payment made in cash other than salary by an employer is known as " allowances". The purpose of payment of these allowances is either to reimburse some of the expenses incurred by the employees or to compensate them a against the effect of increased cost of living. These allowances may be discussed under heads. They are:

I. Allowance fully taxable
II. Allowance partly taxable
III. Allowance not taxable.

I. Allowance fully taxable

Following are some of the examples of allowances which are fully taxable.

1. Dearness Allowance / Dearness Pay (DA/DP)
2. City Compensatory Allowance (CCA)
3. Entertainment Allowance (EA)
4. Fixed Medical Allowance
5. Tiffin/Lunch Allowance
6. Non –practicing Allowance
7. Project Allowance
8. Deputation Allowance
9. Family Allowance
10. Dog Allowance
11. Marriage Allowance/Family Allowance
12. Warden Allowance
13. Over-time Allowance
14. Other Allowances unless specifically exempt

II. Allowances Partly Taxable

1. House Rent Allowance (HRA): This is an allowance paid to an employee to meet expenditure incurred on payment of rent in respect of the house occupied by him for his residence. House Rent Allowance is exempt u/s 10 (13A) to the extent of the least of the following:

a) Actual amount received as HRA.
b) 40% of salary (if the assessee is living in Mumbai, Chennai, Delhi or Kolkata 50% of salary)
c) Rent paid by the employee **Less** least of the above.

Taxable HRA = Actual amount received **Less** least of the above.

Note:1 Salary means, Basic pay + DA (Service benefits) + Commission calculated on turnover at a prescribed rate.

2 No such exemption is available when an assessee is not paying any rent towards the house in which he is living.

3 **No exemption is allowed when rent paid does not exceed 10% of salary.**

Special Allowances to meet the personnel expenses:

Central government has notified certain allowances as exempt u/s 10 (14) (ii) to the extent of **limits** prescribed.

(a) Borders area, Remote locality, Difficult area, Disturbed area allowance exempt upto Rs. 300 p.m. to Rs. 1,300 p.m.
(b) Tribal area / Agency area |Allowance exempt upto Rs. 200 p.m.
(c) Allowance to an employee working in any transport system Rs. 6000 p.m. or 70% of such allowance whichever is less exempt.
(d) **Children Education Allowance**: Exempt @ Rs.100 p.m. per child upto a maximum of two children.
(e) **Children Hostel Allowance** : Exempt @ Rs.300 p.m. child upto a maximum of two children.
(f) Transport Allowance: Exempt upto Rs. 800 p.m. however if the employee is blind or orthopedically handicapped, the exemption is raised to Rs, 1,600p.m.
(g) Underground Allowance: Exempt upto Rs. 800 p.m.
(h) Compensatory field area allowance exempt upto Rs. 2,600 p.m.
(i) Compensatory modified Field Area Allowance Exempt up to Rs. 1,000 p.m.
(j) Counter insurgency Allowance is exempt upto Rs. 3,900
(k) High Altitude Allowance, Exempt upto Rs. 1,060 p.m.
(l) High Active Field Area Allowance is exempt up to Rs. 1,6000 p.m.
(m) Inland Duty Allowance exempt upto Rs. 3,250 p.m.

III. Allowance Not Taxable (Fully exempt)

1. Foreign Allowance: Usually this type of allowance is granted to a government employee posted out side India, or sent on deputation to a foreign country. This allowance may be under different names like Overseas allowance, Children's education allowance Car allowance or Entertainment allowance. Foreign allowance is fully exempt from tax provided the assessee is a (i) Government servant; (ii) an Indian Citizen.

2 Sumptuary allowance to High Court and supreme Court Judges is fully exempt.

3. Allowance from Unified Nations Organization (UNO) to its employee are fully exempt.

Perquisites – Sec. 17(2)

The term 'Perquisite' means any causal emolument, fee or profit attached to an office or position in addition to salary or wages'. Perquisite has a known normal meaning i.e. 'a personal advantage'. It does not cover a mere reimbursement of any expenditure incidental to the employment. Perquisite may be given in cash or kind. To be a perquisite is should be capable of being measured in terms of money. Perquisite may be any benefit or amenity like free use of motor car, rent free accommodation, club bills of the employee paid by employer etc. A perquisite is taxable as salary when it is provided by the employer during the course of employment. Any perquisite received otherwise than from employer shall taxable under the head "income from other sources". Perquisite is taxable irrespective of the particular perquisite is utilized by the assessee or not.

From the Income Tax Act 1961 point of view perquisites may be categorized as

I. Perquisites taxable in all cases of employees.
II. Perquisites taxable in specified cases of employees.
III. Perquisites not taxable.

I. Perquisites Taxable in all Cases of Employees

I. Rent Free Accommodations

Valuation of rent free accommodation/ accommodation at concessional rent depends on the type of the employee. For this Purpose employees are classified into (i) Government employees, (ii) Non-Government employees. Accommodation provided to the employees may be un- furnished or furnished.

Valuation

i) Government employees (These include Central and State Government)

The value of unfurnished accommodation provided to government employees is taken to be rent fixed by the government. This is based on licence fee determined by the government in residences. In the case of furnished accommodation, add either 10% of the cost of furniture or actual hire charges of the furniture as the case may be, to arrive at the value of such accommodation.

Illustration

Mr. Ramana is a government employee. He us provided with a rent fee accommodation at Hyderabad whose municipal value is Rs.80,000 p.a. His pay particulars are: Basic pay Rs. 15,000 p.m. D.A. Rs. 6,000 p.m, BonusRs. 20,000; Entertainment rules is Rs. 1,250 p.m. He is provided with a furniture costing Rs. 60,000. Find out the value of rent free furnished accommodation.

Solution

Mr.Ramana being a government employee, the value of un-furnished accommodation will be as per the government rules, as such –

	Rs.
Value of un-furnished house	15,000
Add: 10% costs of furniture (60,000 x 10%)	6,000

Value of furnished accommodation	21,000
	---------

ii) Other employees

a) Where accommodation is owned by employer:

Un-furnished house

A) City having population exceeding 4 lakhs per 1991 census = 10% salary
B) In other cities = 7.5% salary.

Furnished house

Add: 10% cost of furniture or actual hire charges, as the case may be, to the above value.

b) Where accommodation is not owned by employer OR 10% of salary of employee whichever is less.

Un-furnished house

Actual amount of rent or lease paid by the employer OR 10% of salary of employee which ever is less.

Furnished house

Add: 10% cost of furniture or the actual hire charges of the furniture as the case may be, to the above to, the above value.

Note:1 When in any of the above cases if the employer charges any amount from the salary payable to employee towards the accommodation provided, such facility is known as " Concession Rent Free Accommodation". For this purpose the valuation of the accommodation is to be carried out in a normal way as explained above, and from such value whatever amount charged by the employer towards the accommodation, should be reduced and the balance shall be, the value of concessional rent free accommodation.

2. Salary here means: Basic pay + DA (enters in retirement benefits) + Commission + Bonus + Fees + All other taxable allowances (Except the DA which does not enter into service into service benefits.)

Illustration

Mr. Uday submits you the following particulars : (a) Basic pay Rs. 12,500 p.m. (b) Dearness allowance Rs. 4,500 p.m. (forms part of salary) Bonus 20% salary, Commission Rs. 10,000,Advance salary Rs. 14,000. Entertainment allowance Rs. 6,000, Travelling allowance Rs. 8,000(75% spent on office duties).rent free accommodation owned by employer having a fair rental value of Rs. 75,000 p.a. cost of furniture Rs.80,000. Compute the value of rent free accommodation when-

i) The house is situated in a city having a population exceeding 4 lakhs.
ii) The house is situated in a city not having a popular of 4 lakhs.
iii) The house does not belong to employer, and rent paid was Rs. 2,000 p.m.

Solution

i) House owned by employer ; a city having population more than 4 lakhs.

Unfurnished house: 10% salary	Rs.
Salary = (Basic pay Rs. 1,50,000 + DA (part of salary) Rs. 54,000 + Bonus 20% salary (1,50,000 + 54,000 x 20%)	
Rs. 40,800 = Commission Rs, 10,000 + E.A. 6,000 + TA 25% 2,000) Rs. 2,62,800 and 10%	26,280
Add: 10% Cost of furniture (80,000 x 10%)	8,000
Value of furnished rent free house	**34,280**

ii) House owned by employer; a city not having a popular of 4 lacks.

Unfurnished accommodation	Rs.
7.5% of salary (2,62,800 x 7.5%)	19,170
Add: 10% cost of furniture (80,000 x 10%)	8,000
Value of furnished rent free house	**27,700**

iii) House does not belong to the employer

Unfurnished house	Rs.
Either 10% of salary Rs. 26,280 or rent paid by the employer Rs . 24,000 p.a. whichever	24,000
Add: 10% cost of furniture (80,000 x 10%	8,000
Value of furnished rent free house	**32,000**

Illustration

Taking the problem given in illustration 9, assume that, the employer charges Rs. 2,600 p.m. towards the accommodation provided, compute taxable value of the house is each case:

	Rs.
Case (i) value of furnished house	34,280
Less: Amount charged by employer	31,200
Value concessional rent free house	**3,080**
Case (ii) value of furnished house	27,700
Less: Amount charged by employer	31,200
Value of concessional rent free house	**Nil**
Case (iii) value of rent free house	32,000
Less: Amount paid to employer	31,000
Value of concessional rent free house	**800**

Illustration

From the below given particulars of Umakanth compute the value of rent free accommodation. Basic pay Rs. 96,000 p.a. Dearness allowance Rs. 24,000 p.a. (enters in service benefits) Bonus Rs. 20,000, Commission Rs. 10,000,Advance salary Rs, 12,000, Employer paid the following (i) Life insurance premium Rs 10,000 (ii) Income tax Rs.16,000 (iii) Water electricity bills Rs.8,000. He is provided with a rent free accommodation whose municipal value is Rs. 56,000p.a.,rent paid by the employer Rs. 48,000 p.a. and hire charges of the furniture paid by employer Rs.10,000.

Solution

Unfurnished house

Since the house does not belong to employer the value of rent free unfurnished house will be the least either rent paid by the employer or 10% of salary.

Salary here means: Basic pay Rs. 96,000 + DA (enters in service benefits) Rs. 24,000 + Bonus Rs. 20,000 + Commissions Rs. 10,000= 1,50,000

	Rs.
Thus, 10% of salary Rs. 15,000 or rent by the employer Rs. 48,000 w.e.l.	15,000
Add: Actual hire charges of furniture paid by employer	10,000
Value of furnished rent free house	**25,000**

iv) **Hotel accommodation:** Where any accommodation is provided by an employer to his employee in any hotel, on his transfer from one place to another, and the period of stay does not exceed 25 days in aggregate the value of perquisite shall be NIL. In other cases either the expenditure incurred by the employer or 24% salary (for the period during which such accommodation is provided) whichever is shall be taxable.

v) Accommodation provided in a remote area, the value shall be taken to as NIL. Remote area to an employee is, an employee working at a mining site or an onshore oil exploration site or a project execution site or an accommodation provided in any off shore site of similar nature. Remote area means an area located at least 40 kms away from a town having population upto 20,000

vi) **Dual accommodation in case of transfer:** Where on account of transfer from one place to another an employee may be provided accommodation at bothe the places, then the value of perquisite shall be:

a) **For a period of 90 days:** value of only one accommodation having lower value shall be taxable
b) **For the period after 90 days:** Value of both the accommodations shall be taxable.

2. Any amount paid by employer towards employees life insurance premium.

3. **Any sum paid by the employer in respect any obligation of the employee met by employer.** e.g. club bills, hotel bills, employees loan, children education expenses, wages of domestic servants appointed by employee, car maintenance expenses including driver's salary of a car owned by employee used for domestic purpose.

4. **Interest free or concessional loans:** In case an employer grants interest free or concessional loans they may be valued as under:

a) Where the total of the loan amount does not exceed Rs. 20,000, the value shall be NIL.

b) Where the loan is made for the medical treatment, irrespective of the amount of loan, the value shall be NIL. However any amount is reimbursed by the insurance company, the amount so reimbursed shall be treated as perquisite.

c) Any loan provided by the employer either to acquire a house property or to purchase any vehicle used for conveyance, the value shall be 10% p.a. on the maximum outstanding balance as reduced by the interest if any charged by the employer: e.g. if the employer charges 8% p.a. as interest, the value of perquisite shall 2% of (10% - 8%) out standing balance.

d) Any other loan, the value shall be 13% p.a. on the maximum amount of out standing balance as reduced by the interest, if any, already charged by the employer.

5. **Holidays enjoyment:** The value of traveling, touring and accommodation paid by the employer on behalf of employee, other than leave travel concession, 'LTC', shall be fully taxable.

6. **Free Meals:**

   a) Snacks and refreshments provided during working hours, the value of perquisite shall be NIL.

   b) Free meals provided in a remote area, the value of the perquisite shall be NIL.

   c) Free meals provided at any other place, shall be exempt upto Rs. 50 per meals, any excess of such limit shall be taxable.

7. **Gifts:** Gifts or gift vouchers, (in lieu of which such gift may be received by the employee) given to the employees on social and religious occasions shall be exempt upto and aggregate amount of Rs. 5,000. Excess of this shall be taxable. However gifts made in cash/gift cheques shall be fully texable.

8 **Credit card:** Any expenses charged to a credit card, membership fee, annual fee paid by employer fully chargeable to tax. This applies to an "add on card" also.

9 Club expenses:

a) Corporate membership fee paid employer is not taxable.

b) Any expenses payable by the employee but paid by the employer shall be fully taxable.

10 Use of movable assests: if an employer provides any movable assets like furniture, computer etc., the perquisite is valued as under:

a) If the asset is owned by the employer – 10% p.a. of the actual cost of the asset. Any asset used for more than 10 years by the employer shall not be treated as perquisite.

b) Asset taken on rent – actual hire charges paid by employer shall be taxable.

11 Transfer of movable assests: Where any movable asset belonging to the employer is sold to the employee or any member of his household, at a concessional price the values of benefit shall be

Actual cost of asset to the employer	(-)	Depreciation on origianal cost at 10% for each completed year of use (20 % in case of cars, 50% in case of computers and another electronic items under W.D.V. method)	(-)	Amount paid by the employee.

II Perquisites Taxable in Case of Specified Employees

The following perquisites are taxable in the case of specified classes of employees only, for others they are tax-free. Specified employee means:

a) Director –employee. He is an employee as well as a director in the company in which he is working.
b) Employee having substantial interest in the employer company i.e. holding not less than 20 percent equity shares carrying voting rights.
c) Any other employee whose income is chargeable to tax under the head salaries exceeding Rs. 50,000 Salary here means all monetary receipts employer **Less** deductions u/s 16.

Following are the perquisites taxable under this category.

1. Motor Car

a) Motor Car owned or hired by employer is used wholly and exclusively for official purposes, the value of perquisite shall be **nil.**

b) Car owned or hired by employer is used exclusively for personal use of the employee or any member of his household, and the car running and maintenance expenses are borne by the employer, the value of perquisite shall be, amount actually incurred by the employer + normal depreciation i.e. 10% of the cost of car + drivers's salary paid by employer amount charged from employee.

c) Motor Car is partly used for office and partly for personal purpose

A) If the entire expenses of maintenance and running of the motor car are borne by the employer.

1. Where the cubic capacity of engine does not exceed 1.6 liters: Rs. 1,200p.m.
2. Where the cubic capacity of engine exceeds 1.6 Liter: Rs, 1,600 p.m.

B) If the expense of maintenance and running for his private or personal use met by the assessee himself.

1) Where the cubic capacity of engine does not exceed 1.6 Liters: Rs. 400 p.m.
2) Where the cubic capacity of engine exceeds 1.6 Litre: Rs.600 p.m

<u>Note</u>

In all the above cases, if driver is also provided, an additional amount of Rs. 600 p.m. is added to the value of perquisite.

D) Provision of more than one car: where the employer owns or hires more than one motore car and the employee or any member of his house hold are allowed to use such motor cars, shall be chargeable as under.

i) Value of one car shall be Rs. 1,200 p.m. or 1,600 p.m. as the case may be, for using the car partly for office and partly personal purposes.
ii) Value of other Car/Cars will be taken as if they were used exclusively for private purpose and taxed as per the rules.

e) Car owned by the employee

A) Used wholly and exclusively for office purpose any amount re-imbursed by employer shall not be taxable.

B) Used wholly and exclusively for private use any amount re-imbursed by employer shall be fully taxable.

C) Used partly for office and partly for personal- purpose and expenses are met by employer.

i) For small car Rs. 1,2000 p.m + 600 p.m for driver
ii) For big Car Rs. 1,600 p.m.+ 600 p.m. for driver.

f) Other automotive conveyance other than motor car like scooter, motor cycle etc. provided, the value of such benefit shall be calculated as under.

A) Where the vehicle is exclusively used for office purpose and expenses are met by employer, the value shall be - nil

B) Where the vehicle is used partly for office and partly for private purpose and expenses are met by employer the value of such perquisite shall be the amount paid by employer less Rs. 600 p.m.

Tax Free Perquisites

The following perquisites are tax-free in all cases of amployee:

1. Medical benefits within India

i) Medical benefits within India

a) Any medical treatment provided free of cost to an employee or to any of his family members in any maintained by him fully exempt.

b) Medical benefits is provided from out side source:

A) if it is a Government hospital or recognized hospital fully exempt.

B) In respect of the prescribed diseases or ailments in any hospital approved by chief commissioner fully exempt.

c) Any medical insurance or group insurance paid by employer, or reimbursement of health insurance premium to employee fully exempt.

d) If the medical treatment of the employee or any other member of his done at any hospital, nursing home, or clinic owned by private practitioners or not recognized by the government or IT authorities, the exemption will be limited to Rs. 15,000.

ii) Medical treatment Outside India

a) Expenditure on the medical treatment of the employee or any member of his family outside India.

b) Expenditure on travel and stay abroad of the patient (employee a family member) and one attendant who accompanies the patient, shall be exempt to the following extent.

A) The expenditure on medical treatment and stay abroad shall be exempt to the exempt to the extent permitted by the Reserve Bank of India.

B) Travel expenditure shall be fully exempt provided the gross total income of the employee does not exceed Rs. 2,00,000

2. Rent free house provided at a remote place.
3. Free meals provided at a remote place.
4. Free recreation facilities to emplouyees.
5. Free refreshments to employees during office hours.
6. Telephone/mobile phone bills paid by employer.
7. Issue of shares at discount employees under ‘stick option’ scheme.
8. Perquisites to government employees posted outside India.

9. Leave Travel Concession.
10. Refresher courses, Training courses to employees to keep them abreast of latest knowledge.
11. Gifts in kind upto Rs. 5000 in a year at discount.
12. Free ration to armed personnel.
13. Sale of goods manufactured by employer at discount.
14. Laptops and computers provided for personal use.
15. Interest free loans, an amount not exceeding Rs. 20,000.
16. Provision of newspapers and journals.
17. Education scholarships to the children of employees etc.
18. Free meals up to Rs. 50 per meal.

Profits in Lieu of Salary

Any amount received in place of salary in known as profits in lieu of salary. They include the following

1) Compensation for loss of employment.
2) Any payment from un- recognized provident fund.
3) Any amount received under a keyman insurance policy including bonus.
4) Any amount received or due (in lump-sum or otherwise) from any person before going to any employment with that person or after the cessation of employment with that person.

Provident fund

In order to encourage the habit of saving and providing protection of post retirement life of an employee, provident funds are introduced. Normally certain percentage of salary is contributed to a provident fund by the employee. In India, it has been the practice that employer also makes contribution to employees provident fund. Both contributions get accumulated and an interest is paid on the accumulated balance at a specific rate, which again is credited to the fund. The amount so accumulated over a

Type of provident funds

- i) Statutory Provident Fund (SPF)
- ii) Recognized Provident Fund (RPF)
- iii) Un-recognized Provident Fund (URPF)
- iv) Public Provident Fund (PPF)

Statutory Provident Fund (SPF) : This is the oldest provident funds in India established under Provident Fund Act 1925. This SPF is meant to be maintained by Government and Semi-/Govt. organizations like RBI, SBI, Universities, Corporations etc., for their employees. Under this any contribution made by the employee shall equality fully for rebate U/S 88, employer’s contribution, refund of any amount from such fund and interest credited to SPF is tax-free.

Recognized Provident Fund (RPF) : This fund is normally maintained by private sector employees. Any fund which fulfills conditions laid down in part of the fourth schedule Income-tax Act 1961 and is recognized by the chief commissioners of Income tax.

Employees contribution shall quality for rebates U/S 88. Employer's contribution up to 12% of salary is tax-free any excess of it shall be taxable, refund of any amount from RPF shall also be tax-free provided, the assessee employee has maintained it for a minimum period of 5 years. Interest credit RPF up to 9.5% is tax-free excess is taxable.

Un-Recognized Provident Fund (URPF) : Again this fund is maintained by private sector employers. Any fund which is not recognized by the commissioner is called UPF. Employees contribution does not quality for rebate U/S 88, employer's contribution and interest credited to URPF should be ignored for the timebeing. But when any amount is refunded, of the amount of refund employer's contribution and interest there-on shall be charged to income-tax under the head salaries.

Public Provident Fund (PPF): Under the scheme of this find any individual (Salaries or otherwise) not being minor can open an account at any of the branches of State Bank of India with a minimum contribution of Rs. 100 and maximum contribution of Rs. 60,000 per annum. Contribution to this fund qualifies for rebate U/S 88, interest and refund of amount are tax-free.

The following table can help us in understanding the provisions of various provident funds.

Type of provident Fund	Employer's contribution	Employer's contribution	Interest credit	Refund
1. SPF	Fully qualifies for rebate U/s 88	Tax-free	Tax-free	Tax-free
2. RPF	-do-	Tax-free upto 12% salary, excesss taxable	Tax-free up to 9.5%; excess if any is taxable	Tax-free provided, maintained for 5 years
3. URPF	Does not qualify for rebate U/S 88	Ignore for the the time –being	Ignore for The time being	Employers Share and interest thereon is taxable
4.PPF	Fully qualities for rebate U/S88	Not applicable	Tax-free	Tax-free

Rebate of Income-tax U/S88: A rebate of income tax is allowed regarding qualified savings like, life insurance premium, contribution to provident funds, purchase of national saving certificates etc. For more details read the lesson: rebates and reliefs in the latter part of this book.

Meaning of salary for different purchases

1.Taxable income under the head salary	Basic salary, wages, bonus, commissions, fees, advance salary, arrears of salary, over time remuneration, pension, gratuity, leave encashed, excess of 125 salary contributed by employer towards RPF, Transferred balance, taxable allowances, and perquisites
2 For the calculation of HRA, Gratuiity RPF, Bonus etc.	Basic pay, DA (enters in service the benefits) and commissions on turnover.
3. Entertainment allowance	Basic pay only
4 Rent free accommodation	Basic pay, DA(service benefits), commission, bonus and taxable portion of all allowances except normal D.A
5. Determination specific employee	All monetary receipt by whatever name called less deductions U/S 16, exceeding Rs. 50,000
6. Standard deduction U/S 16(i)	Gross salary less deduction U/S 16 (ii) and 16 (iii)

Deductions from salaries

While computing taxable income from 'salaries' the following deductions are allowed from "**Gross Salary"** U/S 16. Gross salary is the aggregate of various items taxable under salary, allowances, perquisites and profits in-lieu of salary. The word "**Gross Salary**" must not be confused with that of 'Gross Total Income'. These deduction are:

1. Standard deductions U/S 16 (i):

Irrespective of the nature and stature of employment every employee is allowed a deduction U/S 16(i) . This deduction is applicable to pensioners also.

An assessee whose income form salaries before standard deduction is:

a) Upto Rs. 5,00,000 – 40% of such salary or Rs. 30,000 Whichever less.
b) Above Rs. 5,00,000 – Rs. 20,000.

Note: There was no standard deduction from the assessment year 2005-2006.

2. Entertainment allowance U/S 16 (ii)

a) Government employees:
Least of the following is deductible

i) Rs. 50,000
ii) 20% of basic salary
iii) Actual allowance received.

b) Non-Government employees: From the assessment year 2002-03 this deduction to non- government employees is withdrawn.

3. Professional tax U/S 16 (iii)

Tax on employment by whatever name called, levied by State Government Shall be allowed as deduction to a salaried tax-payer.

Illustration

Mr. Banti, a Government employee, draws the following emoluments.

Basic salary Rs 12,000 p.m. D.A. Rs. 4,000 p., Entertainment allowances Rs. 7,000 Traveling allowances Rs. 8,000,(80% of Spent). He is provided with a motor car of 1.6 litre c.c. for free use, all expenses are met by employer. Compute taxable salary for the assessment year 2004-05.

Solution

Computation of income from salary of Mr. Banti for the assessment year 2004

Rs.	Rs.	
Basic pay		1,44,000
D.A	48,000	
Entertainment allowance		7,000
Traveling allowance	8,000	
Less: Spent portion	6,400	1,600
Motor car: small car used for both domestic And office Rs. 1,200 p.m.		14,400
Gross Salary		**2,15,000**
Less: Standard deduction U/S 16 (i)	30,000	
Entertainment allowance U/S 16(ii) Least of the following		
a) Rs. 5,000		
b) 20% basic pay Rs. 28,800		
c) Actual amount received	5,000	35,000
Salary income		**1,80.000**

Illustration

Mr. Ravi working in a private company furnishes the following particulars:
Basic pay Rs. 10,500 p.m.
Dearness allowance Rs. 4,500 p.m. (part of salary)
Commission on turnovers Rs. 9,000
Bonus 105 salary
Entertainment allowance Rs, 8,000
Conveyance allowance Rs. 6,000 (60% spent)
The company has given him a housing loan of Rs. 3 lakhs on 1-4-2003 @ 6% p.a.
Employer paid Rs, 9,000 telephone bills nd life insurance premium of Rs 12,000
Ashok paid professional tax of Rs. 2,400
Computer income from salary.

Solution

Computation of income from salary of Mr. Ravi for the assessment Year 2004-05

	Rs.	Rs.
Basic pay		1,26,000
D.A	54,000	
Bonus 10% salary (1,26,000 + 54,000 + 10,000)		19,000
Commission		9,000
Entertainment allowance		8,000
Conveyance allowance (spent portion 405)		2,400
Value of housing loan (3,00,000 X 4%)		12,000
Life insurance premium paid by employer		12,000

Gross salary		**2,42,400**
Less: Standard deduction U/S 16(i)	30,000	
Entertainment allowance U/S 16(ii)	N.A	
Professional tax U/S (iii)	2,400	32,400

Salary income		**2,10,000**

Note

1. Mr. Ravi being a privates sector employee he is not entitled for deduction U/S 16 (ii)
2. Interest on housing loan is prescribed at 10% p.a., here the different 4% is taxable

Illustration

Mr. Shashikanth submits the following particulars for the financial year 2003-04.

Basic pay Rs. 96,000 p.a., Rs. 44,000 p.a.(Part of salary), Bonus 10% of salaryhouse rent allowance Rs. 24,000 p.a., Rent pid at Hyderbad Rs. 30,000 p.a. He is also provided with a free use of motor car of 1.6 litre Cc all expenses of which are borne by employer including drivers salary. Commission on sales ¼ % of sales (sales achieved during the year Rs.10,00,000). Own contribution to provident fund Rs. 20,000 interest was credited to provident on a balance of Rs. 3,00,000. Compute taxable salary when he is a member of

a) Recognized provident fund
b) Statutory provident fund
c) Un-recognized provident fund.

Solution

Computation of salary income

	RPF Rs.	URPF Rs.	SPF Rs.
Basic pay	96,000	96,000	96,000
DA 44,000	44,000	44,000	
Commission on turnover ¼% of 10 lakhs	2,500	2,500	2,500
Bonus 10% salary	14,250	14,250	14,250
HRA : Least of the following is exempt			
a) Actual amount of HRA Rs. 24,000			
b) 40% of salary Rs. 57,000			
c) Rent paid 10% of slary			
Rs. 30,000 – 14,250 =Rs. 15,750			
Taxable HRA Rs 24,000 – 15,750	8,250	8,250	8,250
Free use of motor car	21,600	21,600	21,600
Employers' contribution to RPF in excess of 12% salary;			
Rs 20,000 – (12% 1,42, 500) 17,100	2,900	---	---
Interest credited to RPF in excess of 9.5% p.a. Rs. 30,000 –(9.5% of Rs.3,00,000)			
Rs. 28,500 1,500	---	---	
Gross Salary	**1,91,000**	**1,86,000**	**1,86,600**
Less:Deduction U/S 16 (i) standard Deduction from (max)	33,000	30,000	30,000
Taxable salary	1,61,000	1,56,600	1,56,600

Note :

Mr. Shashikanth will get a rebate of 15% on provident fund contribution when, he is a member of RPF and SPF.

Illustration

From the following information compute the income from salaries of 'X' and qualifying amount for rebates u/s 88.

i)	Basic salary	1,80,000
ii)	DA	60,000
iii)	City Compensatory Allowance (CCA)	6,000
iv)	Entertainment Allowance (EA)	9,000
v)	Travelling Allowance (fully spent)	12,000
vi)	News paper Allowance (fully spent)	2,400
vii)	Own contribution to RPF	18,000
viii)	Employer's contribution to RPF	18,000
ix)	Interest credited to RPF @ 15%	15,000
x)	Rent fee house at Banglore, the rent of which Rs. 36,000 paid by the company, including hire charges of furniture Rs. 10,000	

xi) His employers reimbursed medical expenses Rs. 18,000, telephone bills Rs. 8,000, leave travel Concession 9,000, club bills 8,000

xii) He is provided with free use of 1.8 litre c.c. motor car Along with the driver for both office and private Purpose. Expenses are met by employer.

xiii) Children of the employee are provided with free education in a school run by employer. Normal expenditure in a school for two children I the same locality will be Rs. 36,000p.a.

xiv) Mr. 'X' Paid the following
a) Repayment of housing loan Rs. 24,000
b) Purchase of National Saving Certificates, VIII issue Rs.12,000

Solution

Computation of salary income of Mr.'X' for the A.Y. 2004-05

Basic Salary	Rs.	Rs.
DA		1,80,000
CCA		60,000
EA		9,000
Employers's Contribution to RPF in excess of 12% salary		
Interest on RPF in excess of 9.5 %		5,500
Rent free house (unfurnished)	19,500	
Add: Hire charges of furniture	10,000	29,000
Motor Car (1,600 + 600) X 12		26,000
Club bills paid by employer		8,000
Children Education Expenses	36,000	
Less 1,000 X 2 X 12	24,000	12,000
Less: Standard deduction u/s 16 (i) (Max)	30,000	3,36,400
Entertainment Allowance 16 (ii)	NA	30,000
Salary income		**3,06,400**

Note

1) Salary for the purpose of rent – free house
1,80,000 + 6,000 + 9,000 = 1,95,000

Since the house does not belong to the employer value of unfurnished house will be either 10% of the salary Rs. 19,500 or actual rent paid by employer Rs. 26,000 which ever is less.

(36,000 – 10,000 hire of furniture)

2) Incase free education is provided by employer in a school by him self, normal expenditure in a similar school less Rs.1,000 p.m. per child is the value of such benefit.

3) Qualified savings u/s 88

	Rs.
Employees contribution to RPF	18,000
Repayment of house building loan	
(restricted to maximum)	20,000
National saving Certificates VIII issue	12,000
	50,000

SUMMARY

The term salary includes various incomes and benefits received by an employee from an employer i.e. Basic Salary, Bonus, Commission Allowance, Perquisites, Profits, in lieu of salary etc.

Allowance means any fixed monetary benefit given to an employee to meet any particular purpose.

Allowances are of three kinds, fully Taxable Allowance, Fully Tax Free Allowances and Partly Taxable Allowances.

Entertainment Allowance is one of the deductions allowed U/s 16(ii) from gross Salary. Entertainment Allowance given by employer for official purpose shall not be treated as income.

House Rent Allowance is given to an employee towards rent of the house. It is a partly exempted allowance and remaining part of the allowance is taxable.

Standard Deduction is a compulsory deduction allowed to an employee drawing income from Salary U/s 16(i).

An employee can claim full amount of professional Tax paid as deduction U/s 16(iii).

Any house of accommodation provided to an employee without rent is called rent free accommodation. The value of the such accommodation is taxable.

Any amount paid to an employee instead of salary it is called a Profit in Lieu of Salary.

Gratuity means the payment made to an employee by the employer for the recognition of his services rendered in the part.

Qualified savings are the savings on which tax rebate is given.

Provided fund is a fund set up for future purposes of an employee they are of four kinds.

a) Statutory Provident Fund b) Recognised Provident Fund
c) Unrecognised Provident Fund d) Public Provident Fund.

QUESTIONS

1) Explain briefly the incomes which are chargeable under the head salaries.
2) What are the important features of salary ?
3) List out any 10 allowances which are fully taxable.
4) Explain the provisions relating to
   a) Standard deduction b) House rent allowance
   c) Entertainment allowance d) Conveyance allowance
5) Define “Perquisites”. List out any 10 perquisites which are fully tax free to all the employees.
6) Explain the method of valuation of the following perquisites.
   a. Motor car
   b. Rent free accommodation.
7) Explain the different kinds of Provident Fund.
8) Explain the different kinds of deductions which are allowed to an employee drawing income from salary Under Section 16.
9) What are qualified savings ? List out any 10 of such savings under section 88.
10) What do you mean by gratuity ? Explain the provisions relating to gratuity ?
11) Define the following as per Income Tax Act.
    a) Allowances b) Perquisites c) Profits in Lieu of Salary
12) Mr. Gurrala Pentaiah is employed in a firm of Bangalore and furnished the following particulars for Assessment Year 2000-2001.
    i) Salary @ Rs.10,000 per month
    ii) Dearness Allowance 50% of Salary
    iii) Own Contribution to RPF Rs.500 per month
    iv) House Rent Allowance per annum Rs.8000
    v) Rent paid Rs.1500 per month
    vi) Free refreshments during office hours Rs.3,600 per annum
    vii) Conveyance allowance Rs.200 per month
    viii) He has paid the donation of Rs.2,500 towards the National Defence Fund set up by the Central Government.

    Compute his total income for the assessment year 2000-2001.
13) Smt. Shylaja is an employee of a company submits the following particulars of her income for the year ending 31.3.2000.

    Basic Salary @ Rs.4000 per month
    Rent free furnished house rent paid Rs.400 per month
    Cost of furniture provided in the house Rs.9000
    Club bills of employee paid by employer Rs.1000
    Entertainment allowance Rs.2000 per annum (Regularly paid by employer since 1952)
    Find out his taxable salary.

8. INCOME FROM HOUSE PROPERTY

Income from house property is the second source of income, the computation of which is given under section 22 to 27.

CHARGEABILITY (Section 22)

The income from house property (houses, buildings etc,) is to be computed under this head. The income under this head is not based upon the actual income from the house but upon the notional income or annual value of that house.

The following points to be noted while calculating the income under the head house property

1) Buildings or land apartment there to : the income derived from buildings or lands attached to the building is taxable. Land which is not attached to any building does not come within the scope of this head. Income from such land is taxable under the head other sources.

2) Annual Value : It is not the rent which is put to tax but the annual value of the house. The annual value will be determined as per the provisions of the section 23 (will be discussed in detail)

3) Owner ship : The income from house property is taxable only in the hands of owner. Income from sub letting will be chargeable under the head.

a) The Assessee has to pay tax not on actual income from house but on notional income or the annual value of that house

b) The Assessee should be the owner of the property. If the right of a house is in dispute the person who receives rent shall be liable to pay tax till the dispute is settled. If any tenant lets out a part of the hired house, income derived from such subletting shall not be regarded as income from House Property but it is taxable under the head Income from other sources. If an assessee carries on business or profession in his own house, the income of such business or profession is taxable under the head income from business or profession. If the house is mortgaged, the person who mortgages is liable to pay tax. If any house or building is constructed on lease lands, the lessee will be considered as the owner for tax purpose.

4) House must not be used for assessee's own business or profession: if the assessee carries on business in his own house, the income is from that house is not taxable. No rent will be allowed while calculating the business income of the assessee.

5) Composite letting of building with furniture: If the building is let out along with the furniture, the income should be divided in to two parts. The income from building is taxable under the head house property and income for the furniture etc., is taxable under the head other sources. If the income cannot be split up as mentioned above, the whole rent will be treated under the head other sources.

6. Quarters let to Employees : If the house is let out to the employees by the employer whose services are essential to the business any rent received will be treated as income from business.

7. Disputed Ownership : In case of dispute about ownership the person who receives the rent shall be liable to pay tax till the dispute is settled.

GROSS ANNUAL VALUE

The highest among the following amounts is treated as Gross Annual Value

1) Municipal Valuation of a House
2) Actual rent received
3) Fair rental value

DETERMINATION OF ANNUAL VALUE

Annual value of property is determined under two major heads.

1. Annual value of let out house property
2. Annual value of self –occupied house property

1. Annual Value of let out house property

Annual value of let out house property explained under 4 different Situation. They are:

a) House property is let out for full year and there is no vacancy period and unrealized rent.
b) House property is let out and there is a vacancy period
   i) If rent actually received or receivable is more than ERV
   ii) If rent actually received or receivable is less than ERV
c) House property is let out and there is unrealized rent
   i) If rent actually received or receivable is more than ERV (After deducting unrealized rent)
   ii) If rent actually received or receivable isles than ERV (after deducting unrealized rent)
d) House property is let out and there are both vacancy period and unrealized rent.

2. Annual value of self – occumpied house property

Annual value of self occupied house property shall be understood under 4 different situations:

a) Only one house under own occupation.
b) More than one house under own occupation.
c) House property consisting of various independent units, one is under self occupation and others are let out.
d) House property is partly let out and partly self occupied.

Basic of computing Income from house property for the Assessment Year 2004-05

		Rs.
Gross Annual value		xxx
Less: Municipal taxes		xxx
Net Annual value		xxx
Less: Deduction under section 24		
i) Standard deduction:		
30% of NAV		
ii) Interest on borrowed capital	xx	
Income from house property	xx	xxx

Gross Annual Value

Step:1 Compare Municipal Rental value (MRV) Fair Value (FRV) higher of the two should be considered as Expected Rent (ER). But this is always restricted to standard rent (lower figure shall be finally selected as ER)

Step2. Compare the expected rent under step 1 with actual rent and higher of the two is considered as GAV

ADJUSTMENTS OUT OF ANNUAL RENAL VALUE OR GROSS ANNUAL VALUE

1. LET OUT HOUSE PROPERTY

a) Compute Gross Annual value

b) Deduct the amount of Municipal/Local taxes actually paid by the owner during the previous year from the Gross Annual Value.

Conditions

- Municipal taxes include service charges such as sanitation cess, sewerage tax or conservancy cess etc.,
- Municipal taxes paid by the owner: allowed as deduction,
- Municipal taxes must have been paid, pertaining to relevant previous year,
- Municipal taxes due but not paid shall not be allowed,
- Municipal taxes paid by the tenant are not allowed.

Net Annul Value: The value arrived at after deducting Municipal taxes from GAV is called as Net Annual Value.

Deductions U/S 24

1. **Standard deduction or statutory deduction U/S 24 (a)**

This is a compulsory deduction to every assessee who has income from let out house. Actual expenditure incurred will not be considered. The deduction is given at a flat rate of 30% of net annual value. When net annual value is nil or negative, standard deduction is not allowed as deduction.

2. **Interest on Loan U/S 24 (b)**

a) Interest on loan taken to purchase, construct, or repair or renovation or reconstruction is allowed as deduction (entire interest).

b) If the interest is paid in India, actual interest amount is allowed as deduction, and if the interest paid outside India, tax is to be deducted at source and can be allowed as deduction

c) Interest on loan is allowed as deduction on due basis also.

d) If interest paid for earlier period is not claimed a deduction, then the same can not be claimed in the current year.

e) Interest paid for delayed payment of interest is not allowed as deduction.

f) Brokerage or commission for arrangement of the loan shall not be allowed

Interest of pre construction period

g) Interest paid or payable for the period prior to the previous year in which the property is acquired is allowed as deduction (in 5 equal installments) over a period of 5 years starting from the year in which the acquisition / construction period means the period commencing on the date of borrowing and ending on (a) March 31 immediately prior to the date of completion of construction or (b) date repayment of loan whichever is earlier.

h) Interest relating to the repay the original loan, intent paid on the news loan shall also be allowed as deduction.

i) If a new loan is taken to repay the original loan, interest paid on the new loan shall also be allowed as deduction.

INTEREST ON LOAN IN CASE OF SELF OCCUPIED HOUSE PROPERTY

In case of self occupied property only one deduction i.e., interest on loan taken for house property is allowed as deduction U/S 24

Conditions

a) If the house loan is taken before 1-4-99

b) If the house loan is taken after 1-4-99

a) If the house loan is taken before 1-4-99

Where the property is purchased, acquired, constructed, repaired, renewed or reconstructed with borrowed capital, before 1-4-99, the deduction is actual interet payable or Rs. 30,000 which ever is less including interest relating to period prior to construction.

b) If the house is purchased or constructed and the loan is taken after 1-4-99

If the assessee satisfies the following conditions then the deduction shall be given to Rs. 1,50,000

i) The loan is taken on or after 1-4-99 either for construction or for purchasing the house
ii) The construction or purchase process should be competed within 3 years from the end of the financial year in which the loan is taken.

c) If the loan is taken either before 1-4-99 or after 1-4-99

Deduction for interest on loan is the least of the following to amounts

i) Actual amount of interest paid or payable

ii) Rs. 30,000

Special note: Prior Construction Interest (PCI)

Interest on loan taken to purchase or acquire the property interest paid for period prior to purchase / completion of construction will be allowed as deduction in five equal annual installments commencing from previous year in which the house consumer is completed. PCI is allowed even in case of self occupied properties also.

II. Annual value of self occupied house property

Situation 1: ONLY ONE HOUSE AS SELF-OCCUPIE FOR RESIDENTIL PURPOSE THROUGHOUT THE PREVIOUS YEAR.

Where he property consists of one house in the occupation of the owner for his owner residence. The Annual Value of such house is NIL if the following conditions are satisfied.

i) The property or any other part, is not actually let out during the previous year
ii) No other benefit is derived there from.

COMPUTATION OF INCOME FROM HOUSE PROPERTY

	Partly letout partly Self occupied	property owned by co- owners	Deemed to be letout
Gross Annual Value (GAV)	Consider them as two Independent units a) Let out unit & b) Self occupied unit a) For Let out unit apply the rules of let house property b) For self – occupied; apply the self occupied rules.	1.ARV 2.FRV compare which-ever is higher Shall be taken as GAV	Apply the rules of Let out House Property
Net Annual Value (NAV)	a) For Let Out : GAV- Muncipal taxes Paid by owner b) For self – occupied: NIL	GAV – Muncipal taxes paid by owner Divided NAV among co-owners.	GAV- Muncipal taxes paid by owner
Deductions U/s 24	a) For let out=NAV- 30% of NAV as standard deduct-tion & Full Value of Interest.	1. Standard de-duction 30% of NAV	1. Standard deduction 30% of NAV
	b) For self-occupied NAV-Interest Rs.30,000 or 1,50,000 as the case may be	2. Interest on Loan taken for house Property Fall value	2. Interest on loan taken for house property. Fall value

Illustration

Determine the net annual value in the following cases for the assessment year 2004-05.

Particulars	I	II	III
Municipal Valuation	40,000	40,000	60,000
Fair rental value	50,000	30,000	55,000
Standard rent	52,500	50,000	NA
Actual rent	40,000	50,000	50,000
Municipal taxes	7,000	6,000	5,000

Solution

Determination o Gross Annual Value for the assessment year 2004-05.

Case I

Expected rent :	MRV	40,000	
	FRV	50,000	which is higher 50,000
	SR	52,500	which ever is less 50,000

Gross annual value : ARV 40,000 : ER or ARV whichever is higher.
Hence GAV = 50,000

Net Annual Value = GAV – Municipal taxes
= 50,000 – 7,000 = 43,000

Case II

Expected rent : 40,000 (higher of the MRV & FRV but subject to SR)

Gross annual value : 50,000 (higher of the ER & ARV)

Net annual value : 44,000 (GAV – Municipal taxes)

Case III

Expected rent : 60,000 (higher of the MRV & FRV but subject to SR)

Gross annual value : 60,000 (higher of the ER & ARV)

Net annual value : 55,000 (GAV – Municipal taxes)

PROBLEMS ON COMPUTING INCOME FROM LET OUT HOUSE

Computation of Income from House Property (Let out) of Mr.________________ for the assessment year ___________________

	Particulas	Rs.	Rs.
I.	Gross Annual Value		xxxxxxx
II.	Less:		
	Municipal Taxes or local taxes if paid by assessee	xxxxx	
	Cost of the facilities provided to the Tenant (lift maintenance, Vehicle parking, night watchman, Salary of gardener etc.,	xxxxx	
	Annual Value		xxxxxxx

III Deduction U/s. 24(1)

1.	Repairs and collection Charges	xxxxx	
2.	Insurance premium	xxxxx	
3.	Ground Rent	xxxxx	
4.	Interest on loan	xxxxx	
5.	land Revenue	xxxxx	
6.	Vacancy allowance	xxxxx	
7.	unrealised rent	xxxxx	xxxxxxx
	Income from House Property		xxxxxxx

Note: Gross Annual Value is the highest of the following three amounts

1. Municipal Rental Value
2. Annual Rental Value
3. Fair Rental Value

EXAMPLE 1

Mr. Nair has a house and the same is let out for Rs. 5000 per annum the municipal valuation of which is Rs. 10,000 per annum

His expenses in respect of the house are as follows.

Municipal Taxes	Rs. 400
Insurance premium	Rs. 700
Collection Charges	Rs. 300
Interest on Loan taken	Rs. 600
Ground Rent	Rs. 150
Land Revenue	Rs. 250

SOLUTION:

Computation in income of Mr. Nair from House Property

	Particulars	Rs.	Rs.
I.	Gross Annual Value		10000.00
II.	Less : Municipal Taxes		400.00
	Annual Value		9,600.00
III.	Deduction U/s. 24(1)		
	1. Repairs and collection Charges (Rs. 9,600x1/4)	2400.00	
	2. Insurance Premium	700.00	
	3. Interest on Loan	600.00	
	4. Ground Rent	150.00	
	5. Land Revenue	250.00	4100.00
	Income from House property		**5500.00**

Note : 1. Real Rent or Municipal value of the house whichever is higher is taken as Gross Annual Value
2. Actual collection charges will not be considered.

EXAMPLE II

Mr. Bose has three houses Their particulars are as follows.

	House 1	House 2	House 3
Municipal Valuation	30000.00	20000.00	24000.00
Actual Rent Received	20000.00	15000.00	20000.00
Fair Rental Value	22000.00	30000.00	25000.00
Repairs and collection cheques	2000.00	1000.00	500.00
Insurance Premium Paid	300.00	500.00	400.00
Municipal taxes paid	1500.00	3000.00	2000.00
Ground Rent	200.00	300.00	400.00

Compute income of Mr. Bose from his house

SOLUTION

Computation of Mr. Bose income from House Property

	Particulars				Rs.	Rs.	
					House 1	House 2	House3
I.	Gross Annual Value				30000.00	30000.00	25000.00
II.	Less : Municipal Taxes				1500.00	3000.00	2000.00
	Annual Value				28500.00	27000.00	23000.00
IV.	Deduction U/s. 24(1)						
	1. Repairs and collection Charges	7125.00	6750.00	5750.00			
	2. Insurance Premium	300.00	500.00	400.00			
	3. Ground Rent	200.00	300.00	400.00	7625.00	7550.00	6550.00
	Income from House property				**20875.00**	**19450.00**	**16450.00**

EXAMPLE 3

Mr. Sunder lal is the owner of a house and the market value of it is Rs. 9000.00 He has let out 1/3 of his house for a monthly rent of Rs. 500.00. He has paid Rs. 1200 as local taxes, 600.00 as insurance premium and Rs. 300.00 as ground rent.

Find out his income from house property.

SOLUTION:

Computation in income of Mr. Sunderlal from House Property

	Particulars	Rs.	Rs.
I.	Gross Annual Value		6000.00
II.	Less : Municipal Taxes	1200x1/3	400.00
	Annual Value		5600.00
V.	Deduction U/s. 24(1)		
	1. Repairs and collection Charges (Rs. 5,600x1/4)	1400.00	
	2. Insurance Premium(600x1/3)	200.00	
	3. Ground Rent (300x1/3)	100.00	
	Income from House property		**3900.00**

Working Notes:
Gross annual value is higher of the following amounts.

a)	Municipal Rental value	9000.00x1/3	3000.00
b)	Actual Rental Value	500x12	6000.00
c)	Fair Rental Value	--	--

2. Municipal Taxes	1200x1/3	400.00
3. Repairs and collection Charges	5600x1/4	1400.00
4. Insurance Premium	600x1/3	200.00
5. Ground Rent	300x1/3	100.00

EXAMPLE 4

Mr. Ram Prased is the owner of a house in Calcutta. The house is let-out on a monthly rent of Rs. 5000 Municipal Taxes 1500.00, Insurance Rs. 500.00, and interest on loan taken Rs. 10,000 and all these expenses are due but not yet paid. The house is vacant for 2 months.

Compute his income from House property.

SOLUTION:
Computation in income of Mr. Ram Prasad from House Property

	Particulars	Rs.	Rs.
I.	Gross Annual Value	5000x1/2	60000.00
II.	Less : Municipal Taxes		--
	Annual Value		60000.00

VI.	Deduction U/s. 24(1)		
	1. Repairs and collection Charges (Rs. 60,000x1/4)	15000.00	
	2. Interest on Loan	10000.00	
	3. Vacancy allowance (60,000x2/12)	10000.00	35000.00
	Income from House property		**25000.00**

Working Notes:

1. Gross Amount value is the higher of the following three amounts.

a) Municipal Rental Value		----
b) Actual Rental value	5000x12	60000.00
c) Fair Rental Value		---

2. Municipal Taxes
   These are allowed as deduction only if they are actually paid
3. Repairs and Collection Charges 60000x1/4 15000.00
4. Interest on loan taken to purchase a house is allowed as deduction on due basis also
5. Vacancy allowance 60000x2/12 10000.00
   A.V. Period of Vacancy/12

PROBLEMS OF COMPUTING INCOME FROM SELF OCCUPPED HOUSE

Where the house is occupied by the assessee for his residential pupose, such house is called self occupied house.

The annual value of Self occupied house shall taken as nil and the income from such house totally exempted if the following two conditions are satisfied.

a) The house is not given on rent during the previous year
b) The assessee has not derived any other benefit from such house.

DEDUCTION UNDER SECTION 24(1) (SELF OCCUPIED HOUSE)

The deductions Under Section 24(1) are not allowed for a self-occupied house. But interest paid on loan taken for the purpose of purchase or construction or ofor repairs is allowed for deduction as per the following rules.

1. Where the house is purchased or constructed and the loan is taken before 1-4-99 the least of the following two amounts is allowed for deduction
   A) Actual Interest paid B)Rs. 30,000
2. Where the house is purchased or constructed and loan is taken after 1-4-99 and purchase or construction is completed before 1-4-2001 the least of the following two amounts is allowed for deduction.
   a) Actual interest paid
   b) Rs. 75,000
   Self occupied house let out for part of the period
   If the self occupied house is let-out for part of the year during the previous year then income from such property will be calculated as mentioned below

1. Calculate gross annual value. Higher of the following three amounts is taken as gross annual value.

a) Municipal Rental Value

b) Actual Rental Value

c) Fair Rental Value

2. Calculate annual value

Annual Value = Gross Annual Value – Municipal Taxes

3. Calculate proportionate annual value for let out period

Proportionate annual value = Annual Value x let out period/12

Allow the deduction under section 24(1)

a) a) Repairs and collection charges ¼ x Annual Value

b) Interest on Loan : Proportionate to the let out period is allowed on deduction

c) Other expenses.

Actual amount incurred is allowed as deduction

4. The deductions under section 24(1) are allowed to the extent of the annual value.

NOTE : In case the assessee has occupied more than one house for his residential purpose only one house will be treated as self-occupied house the remaining house will be deemed to be let out

EXAMPLE 1

Mr. Kutty has constructed a house and it is used for his residential purpose

Year of Construction	1990
Municipal Rental Valuation	Rs. 30000.00
Fair Rental Value	Rs. 20000.00
Municipal Taxes	Rs. 2000.00
Land Revenue	Rs. 1000.00
Rapairs	Rs. 2000.00
Interest paid on loan	Rs. 20000.00

Calculate his income from House propety.

Computation of Income of Mr. Kutty from house property for the assessment year _____

Particulars	Rs.	Rs.
I. Gross Annual Value		NIL
II. Less : Municipal Taxes		
Annual Value		NIL
Less: Interest on Loan		20000.00
Loss from House property		**20000.00**

Working Notes.:-

1. Municipal Rental Value, Fair Rental Value, Should not be considered for self occupied house. Hence the annual value is taken as Nil.
2. No deduction are allowed under section 24(1) except interest on loan. As the loan is taken before 1-4-99, the deduction is the least of the following two amounts.
   a) Actual Interest paid Rs. 20,000
   b) Rs. 30,000

EXAMPLE 2

Mr. John is dong a business in Kurnool. He owns a house and the same is used for his occupation. The other details are as follows.

He has incurred Repairs for	Rs. 1000.00
Municipal taxes	Rs. 10000.00
Interest on Loan	Rs. 15000.00

He has taken the possession of his house from General Insurance Company on 20.05.1999

During the previous year he shifted his business to Hyderabad and living in a rented house and his self occupied house is vacant for the whole year.

Find out his income from house property.

Calculate his income from House property.

Computation of Income of Mr. John from house property for the assessment year ____

	Particulars	Rs.	Rs.
I.	Gross Annual Value		NIL
II.	Less : Municipal Taxes		NIL
	Annual Value		NIL
	Less : Interest on Loan		15000.00
	Loss from House property		**15000.00**

WORKING NOTES

1. As the house is self occupied the annual value is taken as NIL
2. For self occupied house deduction under section 24(1) are not allowed except interest on loan
3. As the loan is taken after 1-4-99 the deduction is allowed out of the least of the following limits
   a) Actual interest aid Rs. 15000.00 Least
   b) Rs. 75,000 Rs. 75000.00
4. If the house is not occupied by the assessee for the reason of employment or business carried on at other places and residing in a rented house, any interest paid on loan taken to construct the house is allowed as deduction under section 24(1).

SUMMARY

- Any Income derived by an assessee from a house or building is taxed under head Income from House Property
- Tax is imposed on the rental value of the house but not on the actual rent received
- Gross Annual value is the highest among the following amounts
- Municipal Rental Value
- Actual Rental Value
- Fair Rental Value
- Municipal value is the rental of the house according to a local authority
- Actual Rental value is the rent actually received from tenant
- Fair Rental value is the rent of similar accommodation in the same locality or similar locality
- Annual value is the value arrived at after deducting Muncipal Taxes and the cost of facilities provided to the tenant
- Certain deductions are allowed U/s 24(1) for computing income from House Property
- Repairs and collections charges is Statutory or compulsory deductions. Actual repairs and collection charges will not be considered
- Irrecoverable rent from the tenant is called unrealised rent.
- Vacancy allowance is calculated as shown below.
- Vacancy allowance = $\frac{\text{Annual Value x period of Vacant}}{2}$
- Incase of Self Occupied house no deductions are allowed U/s 24(1) except interest paid on the loan taken for the construction, purchase is repair of the house
- Joint expenses are the expenses relating to two or more houses
- Joint expenses are divided among the houses as per the instructions given in the problem. If instruction are not given they are divided on the basis of Municipal valuation of the houses.
- Municipal taxes are allowed for deductions if they are actually paid by the owner of the house, Municipal Taxes if paid by tenant are not allowed for deductions.

QUESTION

1. What is meant by income from house property?
2. Explain the important points for computing the income from House Property?
3. What is meant by Gross Annual Value?
4. Explain how gross annual value is calculated?
5. Define Annual Value and explain how it is calculated?
6. List out the deductions allowed under section 24(1)
7. What is Annual Charge and explain different kinds of annual Charges?
8. What is unrealised rent?
9. Explain how vacancy allowance is calculated?
10. What are Joint Expenses and how are they apportioned?
11. How do you determine annual value of self-Occupied House?
12. Mr. Mani owns a house in Hyderabad. The other details of his house are

a) Municipal Rental Value	Rs. 8000.00
b) Fair Rental Value	Rs. 7000.00
c) Insurance Premium paid	Rs. 500.00

d) Local taxes	Rs. 1200.00
e) Interest on loan for construction of a house	Rs. 750.00
f) Repairs	Rs. 800.00

13. Shri Manik Chand has a house at Ranchi. He has let – out the house for Rs.2500 per month. The municipal value of the house is Rs. 20,000 per annum. The rent of a similar building is Rs. 30,000 per annum

The other Expenses:

1. Municipal Taxes Rs. 3000 not yet paid
2. Insurance Rs. 400
3. Ground Rent Rs. 250
4. Interest on loan taken Rs. 600
5. Collection charges Rs. 500
6. Incurred Rs. 600 for the reapair of house
7. The house is vacant for three months during the previous year.

Find out the income from House Propety.

14. Mr. X is the owner of a house property at Khammam. Find out the income from house property from the following particulars
Fair Rental Value Rs. 5000 per month
Municipal Rental Value Rs. 48,000 per month
Actual Rental Value Rs. 60,000 per month
Municipal Taxes 12%
Repairs and collection charges Rs. 2000
Maintenance of lift Rs. 500
Gardener's Salary Rs. 250 per month
Insurance Premium Rs. 800 per annum
Interest on a loan of Rs. 50,000 @ 10% per annum

15. Mr. Janardhan is the owner of a house and the house is used for his residential purpose. The other particulars are as follows.

Actual Rent Received	Rs. 50,000
Fair Rental Value	Rs. 35,000
Municipal Valuation	Rs. 30,000
Collection Charges	Rs. 4,000
Repairs	Rs. 3,000
Fire insurance	Rs. 1,000
Municipal Taxes	8%

Date of completion of house 1-2-1992.
Find out income from self occupied house

16. Mr. Balalji has a building in Guntur and let out for Rs. 8,000 per month. Municipal Rental Value is Rs. 50,000

Gardener's Salary	Rs. 5,000
Lighting Charges	Rs. 6000
Water Charges	Rs. 3000
Insurance premium	Rs. 2000
Repairs	Rs. 30000

Collection Charges	Rs. 3000

Municipal Taxes10%. These taxes are borne equally by owner and tenant/ Calculate his income from House Property.

17. Mr. Bhushan constructed a house and let out for Rs. 2000 per month. The other details are as follows.

1.	Local taxes	Rs. 200
2.	Land Revenue	Rs. 100
3.	Fire Insurance	Rs. 300
4.	Collecting Charges	Rs. 100
5.	Interest paid on loan	Rs. 500
6.	Unrealised Rent	Rs. 300

He has taken all the steps to collect unrealised rent and Income Tax Officer satisfied about his steps taken by him.
Compute his income from house property for the Assessment year.

18. Mr. Jani Owns two houses. The municipal valuation of the first house is Rs. 3,000 and second house Rs. 2,500. The first house is self occupied and the second house is let out for Rs. 250 per month. The expenses in respect of both houses are as follows

	Ist House Rs.	IInd House Rs.
Municipal Taxes	300	300
Land revenue	150	150
Interest on Loan	300	300
Fire insurance premium	200	200
Collection Charges	NIL	200

The second house is vacant for 2 months
Compute his income from House Property.

19. Mr. A is the owner of a House and its details are as follows:

1.	Municipal Valuation	Rs. 20,000
2.	Rent received	Rs. 25,000
3.	Standard Rent as per rent control Act	Rs. 26,000
4.	Repairs	Rs. 1,500
5.	Municipal Taxes	Rs. 2,000
6.	Insurance Premium	Rs. 250

Compute income from House Property.

20. Mr. Anand is owning a house whose Municipal rental value is Rs. 1,000 per month. The house is used for his residential purpose. During the previous year the house is let out for 5 months on a monthly rent of Rs. 800. The other expenses are:-

a)	Insurance Premium	Rs. 250
b)	Land Revenue	Rs. 1000
c)	Annual Charge	Rs. 2500
d)	Municipal Taxes	Rs. 1000
e)	Repairs and Collection Charges	Rs. 2500

Compute his income from House Property.

21. Mr. Paul has a house which is let out on a monthly rent of Rs. 2500. The other details are as follows:-

a)	Municipal Rental Value	Rs. 35,000 P.A.
b)	Rent of Similar Building is	Rs. 40,000 P.A.
c)	Municipal Taxes	Rs. 4,000
d)	Fire Insurance Premium	Rs. 200
e)	Interest on Loan Taken to construct the house	Rs. 6,000
f)	Ground Rent	Rs. 300
g)	Collection Charges	Rs. 500
h)	Repairs	Rs. 3,000

Compute his income from House Property.

22. Compute the income from house property from information given below.

a)	Municipal Rental Value	Rs. 17,000
b)	Rent received during the year	Rs. 26,000
c)	Municipal Taxes (40% paid by tenant)	Rs. 1,800 P.A.
d)	Expenses incurred on repairs	
	I) By owner	Rs. 2,000
	II) By Tenant	Rs. 3,000
e)	Collection Charges	Rs, 2,000
f)	Date of Completion of House 01.06.1993.	

23. Mr. A. Simhareddy is the owner of a house situated at Nagole. It has been let out for Rs. 8,000 per month. The tax payable by the owner comes Rs. 10,000 but the tenant has agreed to pay the tax directly to the Municipality. The land lord however bears the following expenses on tenants amenities.

Water Charges	Rs. 1200
Gardner Salary	Rs. 1000
Lift Maintenance	Rs. 1200
Lighting of Stairs	Rs. 800

The land lord claims the following deductions:

1.	Repairs	Rs, 20000
2.	Land Revenue	Rs. 1000
3.	Collection Charges	Rs. 4000

Compute the taxable income from house property for the current assessment year.

9. INCOME FROM OTHER SOURCES

'Income from other sources' is the fifth and last head of income under the Income Tax Act, 1961. An income which does not specifically fall under the preceding First four heads of income (viz. Income from salaries, Income from house property , profits and gains of business or profession and capital gains) is to be include under this head. And Income may be charged under this head only as a matter of last resort i.e., after it has been tested at each and found inappropriate for inclusion thereunder. In other words, it is residuary head. The following are the tests o be applied for each head of income.

1. Income from Salary

An income that must treated s income from salary should satisfy the master and servant relationship between the employer and employee. Eg.Mr. X is working s lecturer in a college, Income received from the college is included under the income from salary.

If Mr. X also works in another college as a part-time lecturer, remuneration received by hi is not a salary income. It is income from other sources as the master and servant relationship is missing. Infact, it is a contractor and contractee relationship that exists between the payer and receiver. Other examples of salary nature are given hereunder and must be treated as income from other sorces.

1. Income received by teachers/lecturers/ professors for doing examination related work i.e., paper setting, valuation.
2. Salary received by MPs, MLAs and opposition leaders.

2. Income rom House Property

If the assessee is owner of a house property and leaders out for rent, income earned by him is a income from House property. In this case the test is ownership of the house. On the contrary, rent received by subletting the house to the subtants is not an income from House property but income from other sources.

3. Income from Business or Profession

If the income is derived undertaking any business activity it is categorised as business income. If income is derived by a doctor by running a clinic it is an income from profession, but if the doctor is employed in a hospital then the income will be treated as salary income

4. Income from Capital Gains

Income derived by the sale or transfer of capital asset, is the included under the head capital gains. However, the following are not regarded as from capital gains.

1. Distribution of capital assets in kind of HUF to its members at the time of partition
2. Distribution of capital assets in kind on the dissolution a firm.
3. Distribution of assets in kind by a company to its members on its liquidation.

The scheme of taxation of income under the head other sources envisages the study of the following sections.

1. Chargeability Sec.56.
2. Chargebility of income in general Sec. 56(1)
3. Chargeability of income under specific chargeability Sec. 56(2).
4. Computation of Income.

   Deduction u/s 57

   Amounts no deductible u/s 58

   Deamed income u/s 59

   Winning from lotteries u/s 115 BB.

Chargebility (56)

If an income is to be included under income from other sources the following conditions are to be satisfied:

1 There is an income.
2 The income is not exempt from tax under sections 10 to 13A.
3 The income is neither salary income, nor house property income, nor income from business/ profession nor capital gains which are already described earlier.

If the above three conditions are satisfied, income is taxable under section 56 under the head income 'from other sources'.

General Chargeability [56(1)]

Income of every kind shall be chargeable to income tax under this head if it is not chargeable to income tax under any of the first four heads. The following incomes are are generally chargeable under the head income from other sources.

1. Royalties received
2. Directors fee
3. Salary of pension received from a foreign Government
4. Income from subletting of the premises taken on lese
5. Salary received by MPs, MLAs.
6. Examination remuneration received by teachers/lecturers/ professors.
7. Ground rent received.
8. Interest on loan, saving banks or fixed deposits.
9. Agricultural income received from outside India.
10. Gratuitous payment received by a member of the family from a company in which the family had substantial interest.
11. Income from subletting the house property
12. Director's commission for underwriting shares of a new company

13. Rent from a vacant piece of plot (land)
14. Insurance commission
15. Causal incomes
16. Annuity payable under a will, contract, thrust deed.
17. Interest on securities issued by a foreign government.
18. Family pension received by family members of a deceased employee.
19. In case of retirement, interest on employee's contribution if provident fund is unrecognised.
20. Income from undeisclosed sources.
21. Annuity payable to the leader of a trade mark.
22. Income from markets, fisheries, rights of ferry.
23. Income received after discontinuance of business.
24. Income of minor clubbed with income of parents (exemption upto Rs. 1,500 for each child).
25. Pension received from the government as freedom figters.
26. Income from racing establishments.
27. Commission received (eg. Chit fund commission).

However, the following incomes are not taxable under this head.

1. Excess profits tax income Tax department was held to be profit from business.
2. Remuneration received by a director in the capacity of anemployee..
3. Gratuity received by an employee not from the regular employer but from a third party.
4. Remuneration received by a lawyer not from the regular employer but from a third party.
5. Remuneration received by a lawyer in the capacity of an official receiver.

Specific Chargeability [56(2)]

Section 56(1) as described above takes care of the incomes of residue nature and imposes tax on a variety of items as those amounts could not be charged under the First four specific heads. On the other hand section 56(2) charges specified incomes only. The following incomes are included under specific chargeability category under section 56 (2).

1. Income by way of interest on securities.
2. Dividends
3. Any writing from lotteries, cross word puzzles, races the including horse races, card games and other games of any sort or from gambling or betting of any form or nature whatsoever.
4. Income from machinery, plant or furniture let on hire if not charges to tax under the head 'profits and gains of business of profession'.
5. Any sum received by the as the assessee from employees as contributions to any Provident Fund or super annuation 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.
6. Any sums received under a keyman insurance policy including bonus if not taxable as salary or business income.

Interest on Securities [Sec. 56(2)(1d)]

Income by way of interest on securities is taxable under the head 'Income from other sources". If the same is not taxable as business income under section 28. But then, what is a security ?

"A security is a document acknowledging the debt by a specific authority from general public. It may be named as a Debt, Loan, Paper, Debenture, Bond, or Security or Certificate. It is secured in some manner. A mere debt is not a security unless and until it is secured."

Contents of Security

It contains face value of security, date of maturity rate of interest, date, place and period of payment of interest.

Who can Issue a Security

Securities may be issued by the following authorities.

1. The Central Government
2. State Government
3. Local authority
4. Company
5. Statutory Corporation

Interest on Securities

According to Section 2 (28B) Interest on Securities means :

a) Interest on security of the Central Government or State Government.

b) 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 central or State or Provincial Act.

When an investor invests his money in the bonds issued by Government/Local Authority/Corporations or debentures issued by a Limited Company, the interest received from them is considered as income from interest on securities.

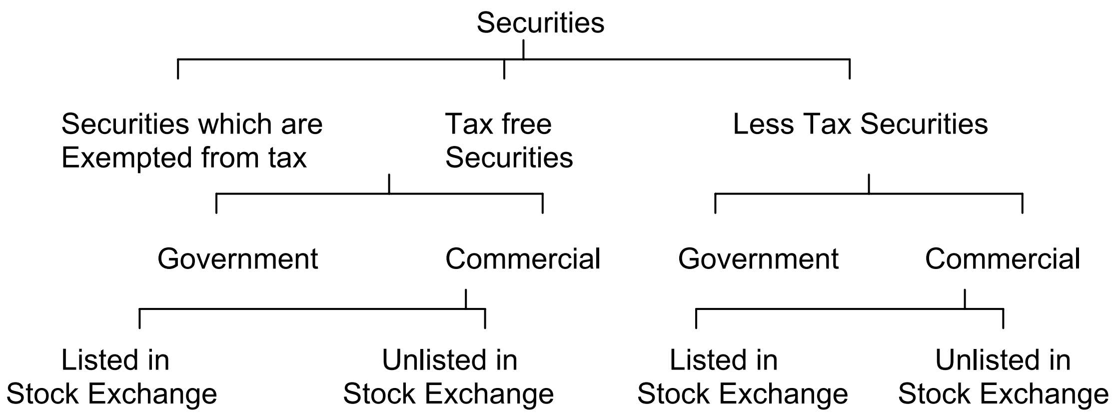
Types of Securities

Securities are issued by Companies, Government – both Central and State, Local authorities are also eligible to raise funds by issuing securities. Following are the types of securities which are currency in operation.

a) Securities issued by Central Government
b) Securities issued by State Government
c) Debentures and bonds issued by local authority
d) Debentures and bonds issued by corporations
e) Debentures issued by companies.

From the tax point of view securities are classified into three types. They are :

1) Securities which are exempted from tax
2) Tax-free securities
3) Less-tax securities



Securities exempt from tax

According to section 10(15) interest on these securities is fully exempt from tax and does not form part of total income of an assessee. In other words it is not taken into account in computing total income. Under section 10(15) (I) the Central Government by notification specifies these securities, bonds etc. The following are the securities which are exempt from tax :

1. Treasury Savings Deposit Certificates
2. Post Office Cash Certificates
3. National Plan Certificates (10 years)
4. National Plan Savings Certificates (12 years)
5. Post Office National Savings Certificates (12 years / 7 years)
6. Post Office Savings Bank (POSB) Account
7. Post Office CTD (Interest upto Rs.5,000)
8. Interest on 9 per cent Relief Bonds
9. Interest on securities held by the Welfare Commission, Bhopal Gas Victims.
10. Interest on notified bonds issued by a local authority/public sector enterprises etc.

Summary of Grossing up

	Nature of security	Grossing up
1.	Tax free Govt. Security	Interest received is gross interest no grossing up.
2.	Tax free Commercial Security (listed)	Grossing up should be done. Gross interest = Net interest x $\frac{100}{90}$
3.	Tax free Commercial security (unlisted)	Grossing up should be done Gross interest = Net interest x $\frac{100}{80}$
4.	Less Tax – Government	Grossing up should be done Gross interest = Net interest x $\frac{100}{90}$
5.	Less Tax Commercial (listed)	Grossing up should be done Gross interest = Net interest x $\frac{100}{90}$
6.	Less Tax Commercial (unlisted)	Grossing up should be done Gross interest = Net interest x $\frac{100}{80}$

Computation of Income from Interest on securities under the head income from other sources for the assessment year 2004-2005 is done as shown below :

		Rs.
1.	Interest tax free Government Securities	xxx

Face value of security x $\frac{\text{Interest Rate}}{100}$

2.	Interest on tax free commercial securities (listed)	xxx

Net interest = Face value x $\frac{\text{Interest Rate}}{100}$

Gross interest = Net interest x $\frac{100}{90}$

3.	Interest on tax free commercial securities (unlisted)	xxx

Net interest = Face value x $\frac{\text{Interest Rate}}{100}$

Gross interest = Net interest x $\frac{100}{80}$

4.	Interest on less tax Government securities		xxx
5.	Interest on less tax Commercial securities		xxx
6.	Interest on less tax Commercial securities (unlisted)		xxx
	Gross interest		xxx

Less : Deductions u/s 57

1) Collection charges	xxx	
2) Interest paid on loan taken to purchase the securities	xxx	xxx
Income from interest or securities		xxx

Illustration

Vikas held the following investments.

a) Rs. 90,000 – 10% (Tax-free) debentures of listed company.
b) Rs. 50,000 – 12% (Tax-free) Punjab Government loan
c) Collection charges Rs. 2,000

Compute his income from interest on securities for the year ending 31.03.2004.

Solution

Computation of Mr. Vikas's income from interest on securities for the Assessment year 2004-05.

		Rs.
a)	Rs.90,000 – 10% (Tax free) Debentures (listed)	10,000
	90,000 x 10% = $\frac{90,000 \times 100}{90}$	
b)	Rs. 50,000 – 12% (Tax free) Punjab Government Loan :	
	50,000 x 12%	6,000
	(Gross Interest)	16,000
Less :	Deductions u/s57	
a)	Collection charges	2,000
	Income from interest on securities	14,000

Working Notes

1. Tax free Commercial securities must be grossed up.
2. Tax free Government securities should not be grossed up because there is no TDS on a security issued by Central or State Government securities.

Illustration

Mr. Kushal holds the following securities on April 1, 2003

Rs.1,00,000 – 5%	Up Government Loan (Date of payment of interest : January 1)
Rs. 40,000 – 6%	Unlisted debentures of ABC Ltd. (Date of payment of Interest : June 1)
Rs. 25,000 – 8%	Debentures of Z Ltd. (Date of payment of interest : June 30, December 31)

On December 1, 2003 he sells 25,000 – 8% debentures of Z Ltd. Calculate the taxable income of Mr. Kushal for the Assessment Year 2004-05 : Business Income is Rs.64,000 ; Collection charges Rs.1,000.

Solution

Computation of Mr. Kushal's income from other sources for the Assessment year 2004-05.

	Rs.
1,00,000 – 5% Up Government Loan	5,000
40,000 – 6% Debentures of ABC Ltd.	2,400
25,000 – 8% Debentures of Z Ltd. Rs. 2000 x ½	1,000
	8,400
Less Deductions : Collection charges	1,000
Interest on securities	7,400
Add : Income from Business	64,000
	71,400
Less : Deduction under section 80L in respect of interest on UP Government Loan (Maximum limit Rs.15,000)	5,000
Net Taxable Income	66,400

Winning from Lotteries, Cross word puzzles, Horse races and Card games etc. [See 56(2)(1b)]

Winning from lotteries, cross word puzzles, races including horse races, card games and other games of any sort or from gambling or betting of any form or nature whatsoever is taxable under section 56 under the head "Income from other sources".

Only winning from lotteries, races, gambling etc., is chargeable to tax. If a receipt is not winnings then it is not taxable under section 56(2)(1b). By virtue of section 115 BB gross winnings from lotteries, cross word puzzles, races including horse races, card games etc. are chargeable to income tax at a flat rat eof 30% **plus** 10% surcharge. From the Assessment Year 2004-05, there is no surcharge if the income does not exceed Rs.8,50,000 in case of individuals/HUF/BOI/AOP.

Under Section 194 B and 194 BB tax is deductible at 30% **plus** 10% surcharge on payments in respect of winnings from lotteries exceeding Rs.5,000. In case of winnings from races including horse races payments exceeding Rs.2,500 are subject to tax deduction at source at the rate of 30% **plus** 10% surcharge.

If the net amount received is given, then the net amount shall be grossed up to find out the amount chargeable to tax. Suppose an assessee derives an amount of Rs.10,00,000 from winnings from lottery or horse race. He may receive a net income of Rs.6,70,000.

	Rs.
Winnings from lottery or horse races	10,00,000
Less : Tax deducted at source 30% + 10% of 30% as surcharge	
Total Tax = 30 + 3% = 33%	3,30,000
	6,70,000

If it is given that, assessee received Rs.6,70,000 (net) on account of winnings from lotteries, then the net receipt shall be converted into gross amount by using the following formula.

$$\text{Gross Amount} = \frac{\text{Net amount}}{(1 - 0.30 + \text{Surcharge as the case may be})}$$

For the assessment year 2004-05 surcharge rates are given below :

		Surcharge
a)	If the tax payer is an individual / HUF / BOI / AOP	
	- If the net income does not exceed Rs. 8,50,000	NIL
	- If the net income exceeds Rs.8,50,000	10%
	- On LTCG and casual incomes	10%
b)	If the tax payer is an artificial judicial person	10%
c)	If the tax payer is a firm, company, cooperative society or local authority	2.5%

Deductions in respect of other incomes u/s 57(ii)

Deductions under this section will be allowed only if the following conditions are satisifed.

a) The expenditure is laid out wholly and exclusively for the purpose of earning such income. If the purpose of earning income is coupled with some other extraneous purpose. It will not be possible to say that the deduction u/s 57(iii) is earned by the assessee.

b) It is not in the nature of capital expenditure.

c) It is not a personal expenditure.

d) It is incurred in the accounting year itself and not in any prior or subsequent year.

Amounts not deductible (U/s 58)

The following amounts shall not be deducted in computing income chargeable under the head "income from other sources"

1. Personal expenses
2. Wealth tax
3. Any interest chargeable under this act which is payable outside India and from which income tax has not been paid or deducted at source.
4. Any payment which is chargeable under the head salaries if it is payable outside India unless tax has been paid thereon or deducted therefrom at source.
5. No deduction shall be allowed in respect of winnings from lotteries, cross word puzzles, card games, races including horse races, gambling, betting etc. However, expenses incurred on owning and maintaining the race horses shall be allowed as deduction.

SUMMARY

Any taxable income which does not find place under any of the first five heads of income is to be included under the head "INCOME FROM OTHER SOURCE" under the Sec. 56(1).

The following are the important incomes to be included under this head.

- Interest on Securities issued by a foreign Govt. on bank deposits, and also on securities.
- Dividends on shares on the share of Co-operative Society.
- Interest on debentures issued by Co-operative Society Clubs etc.
- Winning from Card Games, lotteries, Cross World Puzzles, races, etc.

- Any sum received by the assessee from his employer as the contribution to any staff welfare scheme.
- Rent from lands subletting house, rent or live charges received by Plant Machinery or Furniture etc.
- Examination remuneration received by teacher/lecturer.
- Salary received by MPs and MLAs
- Annuity received by lending trade marks or copy rights.
- Agricultural income from farm lands.

THESE ARE DIFFERENT TYPES OF SECURITIES

I. GOVERNMENT SECURITIES

1. Less tax or General securities
2. Tax free Government Securities

II. COMMERCIAL SECURITIES

1. Less Tax or General Commercial Securities
2. Tax Free Commercial Securities

The dividends which were declare by the Company before 01.06.1997 is treated as Income from other sources and if declared after 01.06.1997 then it becomes an expected income.

Some of the following other incomes which comes under head “INCOME FROM OTHER SOURCES” are

1. Letting of Plant Machinery or Furniture
2. Family pension received by the legal heirs of a declared employee
3. Income from undisclosed sources.

QUESTIONS

Short Questions

1. State any two incomes which are to be included under the had “Income from other Sources”.
2. State any two incomes from interest on Securities ?
3. Write any two incomes from interest on securities which does not come under the thread Income from other sources ?
4. What is dividend on share ?
5. Write some of the other incomes which come under the head “Income from Other Sources”?

Essay Questions

1. Explain the incomes which are to be included under the head Income from other Sources ?
2. Explain the different types of securities ?
3. State the provisions with regard to the dividends secured by an assessee whose status is an individual ?

Problems/Practicals

1. Dcompute the income from interest on securities of Sri. Shashikanth for the previous year ended 31st March, 2000.
   a) Rs. 40,000, 2% Tax Free Government Securities.
   b) Rs. 10,000, 4% Less Tax Government Securities.
   c) Rs. 10,000, 4% Fixed Deposit with state Bank of Hyderabad.
   d) Bank charges Rs.200/-.

2. Compute the income from interest on securities of Mr.Pentaiah, Sr. Asst. for the previous year ended 31st March, 2000.
   a) Rs. 40,000, 6% Preference shares of a Company.
   b) Rs. 20,000, 4% Less Tax Government Securities.
   c) Rs. 10,000, 6% Tax Free debentures of a Public Limited Company
   d) Bank Charges Rs. 100/-.

3. Calculate the income from interest on securities of Mr. Narayana for the assessment year 2000-2001.
   a) Rs. 25,000, 5% Municipal Bonds.
   b) Interest on Tax Free Indian Government Securities Rs. 4,000
   c) Rs. 2,250 Interest on Debentures of Ram & Company (Listed)
   d) Bank Charges Rs.100/-

10. DEDUCTION FROM GROSS TOTAL INCOME

While computing the total income of an assessee some deductions are allowed from the gross total income in addition to deductions that are allowed under different heads of income. These deductions are allowed under section 80CCC to 80U.

The following are some of the deductions admissable to an assessee whose status is an INDIVIDUAL as per prescribed syllabus

Sl. No.	Section
1.	80CCC
2.	80D
3.	80L
4.	80E
5.	80G

80 CCC: CONTRIBUTION TO PENSION FUND

The conditions are:

1. Any individual (whether resident or non-resident, Indian citizen or foreign citizens) is eligible to claim this deduction.
2. Payment is to be made under an annuity plan of the Life Insurance Corporation of Indian or any other insurer (from assessment year 2002 –03) for receiving pension
3. The amount is paid our of income chargeable to tax (Whether of the current year of any earlier year)
4. If the assessee of the nominee surrenders such annuity plan before its maturity date, then the hands of the assessee or the nominee, as the case may be, in the year of receipt.
5. The amount received by the assessee or his nominee by way if pension shall be taxable in the hands of the assessee of the nominee, as the case may be in the year of receipt.
6. This deduction is available to the assessee provided he does not claim such payment for rebate under section 88 of the Act.

Eligible deduction is:

The assessee shall be allowed a deduction under this section to the least of the actual amount so paid or Rs. 10,000. In case the person insured is a senior citizen, then the maximum amont allowance is Rs. 15,000.

SECTION 80D

DEDUCTION IN RESPECT OF PREMIUM PAID BY CHEQUE FOR INSURANCE ON THE HEALTH OF THE SELF AND DEPENDENTS (SECTION 80D)

CONDITIONS TO BE SATFISFIED

i) The scheme of insurance should be of General Insurance Corporation of India and approved by the Central Government.

ii) The policy should be taken
   a) On his health or on the health of his spouse or dependent parents or dependent children and
   b) In the case of HUF or ADP or body of individually consisting only of (in either case) husband and wife governed by the system of community of property in force in the Union Territories of Dadra and Nagar Haveli, Goa, Daman and Diu, on the health of any member of such family, allocation or body of individuals

iii) The premium is paid by the assessee by Cheque Deduction:
   Least of the following two alternatives
   a) Actual insurance premium paid or
   b) Rs. 10,000

   From the ASSESSMENT YEAR 2000 – 2001 where the assessee or his wife or husband or dependent parents or any member of the family is a senior citizen then the limit is raised to Rs. 15,000

80L: INTEREST ON BANK DEPOSIT, CERTAIN SECURITES, ETC.

The conditions are:

1. Any individual or HUF can claim this deduction.
2. If the income is derived from any asset held by, or on behalf of, a firm, an association or persons or body of individuals, the deduction under this section will not be allowed in respect of such income to such partner of the firm or such member of association or body of individuals.
3. In the case of interest on reinvestment deposit scheme, recurring deposit scheme, cash certificate, etc., the interest for each year calculated at the stipulated rate will be taxed as income accrued for the respective previous year.
4. The following are the eligible incomes this sections:
   a. Interest on securities of Central / State Government.
   b. Interest on National Savings Certificate VIII Issue.
   c. Interest on notified debentures issued by an institution or authority or any public sector company or any co-operative society (Including land mortagage bank or a co-operative land mortgage bank.
   d. Interest on National Deposit Scheme, 1984.
   e. Interest on deposits under notified schemes, viz. Post Office (Time Deposits), Post Office (Recurring Deposits) and National Savings Scheme, 1992.
   f. Interest on deposits under Post Office Monthly Income Account Rules, 1987.

g. Interest on deposits with a bank including interest on savings bank account.
h. Interest on deposits with any work bank established by or under any law.
i. Interest on deposit with a financial corporation engaged in providing long-term finance for industrial development in India.
j. Interest on deposits with any housing development authority/board.
k. Interest on deposits with a co-operative society, made by a member with the society.
l. Dividends from a co-operative society.
m. Interest on deposits with an Indian public company, having main object of carrying on business of providing long- term finance for construction or purchase of houses in India for residential purpose.

Note: Interest on debentures of and deposits in companies (other than those specified above) are not eligible for deduction.

Eligible Deduction is:
1. Maximum of Rs. 12,000 for all eligible and incomes and
2. An additional amount of Rs. 3,000 exclusively for interest on Central/State Government securities.

80E: REPAYMENT OF LOAN TAKEN FOR HIGHER EDUCATION

The conditions are:
1. An individual assessee who has taken a loan from any financial institution or any approved charitable institution for purpose of pursuing his higher education is eligible to claim this deduction.
2. The higher education shall be full-time studies for any graduate or post-graduate course in engineering (including architecture), medicine, management or for post-graduate course in applied sciences or pure sciences including mathematics and statistics.
3. The deduction will be allowed from the year the assessee starts repaying the loan and will be available for a maximum period of 8 years or till the loan together with interest is liquidated, whichever is earlier.
4. Repayment of loans taken by the parents for the higher education of their child is not eligible for deduction.
5. The amount shall be paid by the assessee out of his taxable income, by way of repayment of loan or interest thereon.

Eligible deduction is the actual amount paid by the assessee, subject to a maximum of Rs.40,000.

80G: DONATION TO CERTAIN FUNDS, INSTITUTIONS, ETC.

The conditions are:
1 All assessee can claim this deduction.
2. The donation shall be made during the relevant previous year.
3. The donation shall be made to the specified funds or charitable institutions.

4. Proper proof of payment must be submitted to claim the deduction.
5. In a case where an assessee has claimed and has been allowed any deduction under this section in respect of any amount of donation, the same amount does not again quality for deduction under any other provisions of the Act for the same or any other assessment year.
6. Donations made in kind are not allowed for deduction.

Eligible deduction is calculated as follows :

1. Donations must be made to
i) National Defense fund set up by the central Government.
ii) Jawaharlal Nehru Memorial Fund.
iii) Prime Minister's Drought Relief Fund.
iv) National Children's Fund
v) Indoor Gandhi memorial Trust
vi) Africa (Public Contribution – India) Fund
vii) National Foundation for communal Harmoney
viii) Approved Universities/Educational Institutions of National eminence.
ix) Chief Minister's Earth quake Relief Fund, Maharashtra
x) Prime Minister's National Relief Fund
xi) Prime Minister's Armenia Earth quake Relief Fund
xii) Rajiv Gandhi Foundation
xiii) Zila Sakshrata Samity – The Zial having population not exceeding one lakh
xiv) Government or any approved local authority, institution or association to be utilised for the purpose of promoting family planning
xv) Rural Development fund set up and notified by the central Government
xvi) Trust or institution of National importance which as its main object the undertaking of scientific research or carrying on of any programme of conservation of natural resources.
xvii) Government or any local authority to be utilised for any charitable purpose
xviii) Any notified temple, mosque, gurudwars, church, or either palce (for renovation or repair)
xix) Any corporation established by the central Government or any State Government for promoting interests of the members of minority community. Minority community means a community notified as such by the central Government in the official Gazette to in this behalf.

2. Minimum qualifying amount:
a) The following donation made to donees (i) to (Xiii) will qualify in full
b) The following donations made to donees (xiv) to (xix) should not be more than 10% of the gorss total income as reduced by the deductions available under section 80D to 80U excluding 80U donations in excess of 10% of the adjusted gross total income will be ignored while computing the aggregate of the sums in respect of which deduction is to be allowed.

3. Only donations made in cash and not kind will qualify for deductions.
a) 100% of the qualifying amount of donations made to doneees as mentioned in (vi) to (xi), (xiii) and (xiv) above
b) 50% of the qualifying amount in case of others.

Deductions in respect of Incomes

Section	Particulars of deduction	Extent of deduction allowed
800HHB	Profits and gains from projects outside India	10% of such profits
80HHBA	Profits from hosing projects	10% of such profits or amount credited to Housing Project Reserve A/c. whichever is less
80HHCq	Profits and gains from export business	30% of export proceeds
80HHD	Profits in convertible foreign exchange from hotel business travel agency	(i) 15% of profits, and (ii) Amount credit to reserve account not exceeding 15% of profits
80HHE	Profits from emport of Computer Software	30% of such profits
80HHF	Profits from export of Film Software etc.	30% of such profits
80-IA	Profits of undertakings engaged in infrastructure facility	a. Telecommunication services i) 100% of Profits for first 5 years ii) 30% of profits for next 5 years b. Others : 100% of profit for 10 years
80-IB	Profits of business engaged in non infrastructure facilities	i) 25% to 100% ii) 8 years to 12 years
80-IC	Profits and gains from certain undertaking or enterprises in the states of Himal Pradesh, Uttaranchal, Sikkim and North-Estaern States	100% of profits for first 5 years and 25% of profits for next 5 years
80JJA	Profits of bio-degradable waste	100% of profits for 5 years
80JJAA	Employment of new workmen	30% of additional wages for 3 assessment years including the A.Y. relevant to year of employment
80 L	Interest on bank deposits and government securities,etc.	Upto Rs. 12,000, plus Rs. 3,000 for Government securities
80LA	Certain incomes of offshore banking units in special economic zones	100% of specified income for first 3 years and 50% for next 2 years
80-0	Income from patent, etc., received by an Indian company or other residents in India from certain foreign enterprises	10 % of such income
80- QQB	Royalty to authors	a) If received in limpsum 100% of royalty upto a maximum of Rs. 3 lakhs. b) If not received inlimpsum 15% of value of books sold during previous year.

80R	Remuneration from certain foreign resources to teachers who are Indian citizens	15% of such remuneration brought into India under FERA within 6 months from end of previous year
80PP	Professional income form certain foreign sources to authors, etc.	-D0-
80RRA	Remuneration received from foreign or Indian employers by Indian technicians working outside India	-Do-
80RRB	Royalty on patents	100% of royalty upto a minimum of Rs. 3 lakhs
80U	Blind or handicapped person or mentally retarded persons	Rs. 50,000

Deduction in Respect of Payment,etc.

Section	Particulars of deduction	Extent of deduction allowed
80CCC	Contribution to Pension Fund	Maximum Rs. 10,000
80D	Health insurance premia	Maximum Rs.10,000, and Senior-Citizens – Maximum Rs. 15,000
80DD	Medical treatment etc. and deposit made for maintenance of handicapped dependent	Rs. 50,000, and for servere disability Rs. 75,000
80DDB	Medical treatment of specified diseases	Rs 40,000, and for Senior Citizens Rs. 60,000
80E	Repayment of loan taken for higher education	Maximum Rs. 40,000
80G	Donation to certain funds, institution, etc.	Donations in cash only allowed, deduction to the extent of 50% and in certain cases 1000% of the qualifying amount of donation is allowed.
80GG	Expenditure on house rent incurred by self-employed persons.	Upto Rs. 2,000 per month.
80GGA	Donations for scientific research or social or statistical research or rural development, etc.	100% of qualified expenditure
80GGB	Contribution by companies to political parties	100% o of donation made
80GGC	Contribution by any person to political parties	100% of donation made

Illustration

X is lawyer of Delhi High Court. He keeps his accounts on cash basis, His receipts and payment accounts for the year ending 31st March 2004 is given below:

	Rs.		Rs.
Balance b/d	3,820	Subscription and membership	5,800
Legal fees	1,46,000	Purchases of legal books	7,500
Special commission fee	5,500	Rent	47,500
Salary from Law College as part-time Lecturer	27,000	Office expenses	8,500
Exam remuneration	1,480	Electricity expanses	4,000
Interest on bank deposits	3,500	Income tax	8,000
Sale proceeds of residential property	2,51,000	Gift to daughter	12,000
		Domestic expenses	25,000
Dividend from co-operative society	1,000	Donation to institutions approved u/s 80 G	2,000
Dividend received from Units	2,000	Car purchased	2,20,000
		Life insurance premium	6,000
Rent from house property	15,000	Balance c/d	1,10,000
	4,56,300		4,56,300

Further information is available

a. The rent and electric expenses are related to a house, of which half portion is used of self-residence and the remaining half portion is used for office.

b. Car is used only for professional purposes car expenses Rs14,000 Depreciation on car Rs.44,000.

c. Outstanding legal fees Rs. 10,000.

d. Rent has been paid for 10 months only.

e. Car was purchased on 25-9-2003, Law books purchased are annual publications out of which books of Rs. 2,000 were purchased on 6-4-2003 and balance 31-10-2003.

f. The house was purchased In January 1984 for Rs,. 50,000 and sold on 1-7-2003.

g. Rent of the property which has been sold was Rs. 5,000 p.m. The tenant vacated the property on 30-6-2003. Sale proceeds of residential property is to be less with Rs. 1,99,569.

Determine his total income for the assessment year 2004-05.

Solution

Computation of Total Income of Mr. X for the assessment year 2004-05

	Rs.	Rs.	Rs.
Income from Salaries			
Salary as a part-time lecturer		27,000	
Less: Standard deduction @ 40%		(-) 10,800	
			16,200
Income from House Property			
(Gross annual value 5,000 x 12= Rs. 60,000)			
Proportionate for 3 months 60,000 x 3/12		15,000	
Less: Municipal taxes		---	
Net annual value		15,000	
Less: Statutory deduction @30%		(-) 4,500	
			10,500
Income from Profession			
Legal fees		1,46,000	
Special commission		5,500	
		1,51,500	
Less; Allowable expense:			
Subscription etc.	5,800		
½ Rent (Office)	23,750		
Car expenses	14,000		
½ electric charges	2,000		
Office expenses	8,500		
Depreciation on car	44,000		
Depreciation on books	4,750		
		(-) 1,02,800	
			48,700
Capital gains			
Sale consideration		2,51,000	
		(-) 1,99,569	
			51,431

Income from Other Sources

Interest on Bank deposit	3,500	
Examiner's fees	1,480	
Divided from co-operative society	1,000	
Dividend from UTI	Exempt	
	---------	5980

		1,32,811
Gross total income		
Less: Deductions		
U/s 80G – Donation @ 50% on Rs. 2,000	1,000	
U/s 80L – (3,500 + 1,000)	4,500	

		(-) 5,500

TOTAL INCOME		1,27,311

Notes

1. As the assessee follows the cash system of accounting, amount actually received and payment actually made on account of expenditure , during the year, shall be considered for computing the home income. Therefore, any outstanding receipts will not be included in the Total Income. Similarly, rent not paid for two months will not be allowed as deduction.

2. The system of accounting not effect the computation of income from salary, house property and capital agains. Therefore, in this case, rent three months, though not received (as it has not been shown in the Receipts and Payments Account) shall be taken into account in computing the income under the house property.

3. Car was purchases and put to use for more than 180 day. Therefore, full depreciation @ 20% has been claimed.

4. Law books worth Rs. 2,000 were purchased and put to use for more than 180 days and are, there for, eligible for depreciation @ 100%. The balance books worth Rs. 5,500 were purchased on 31- 10 – 2003 ; therefore, 50% of the normal depreciation will be allowed as the books were purchased and put to use for less than 180 days. The total depreciation shall, therefore, be Rs. 2,000 + 50% of Rs. 5,500 = Rs. 4.750.

5. The assessee shall be eligible for rebate u/s 88 @ 20% on life insurance premium of Rs. 6,000, i.e., Rs. 1,200.

SUMMARY

- While computing the total income of an assessee some deductions are allowed from the gross total income in addition to deductions that are allowed under different heads of income.
- These deductions are allowed under section 80CCC to 80U

Explain the following deductions from the Gross Income

1. Sections 80CCC
2. Sections 80D
3. Sections 80L
4. Sections 80E
5. Sections 80G

PROBLEMS/PRACTICALS

1. X is the manager of Y Co. Ltd. He furnish the following particulars of income for the previous year 2003-04.

   Basic Salary Rs. 36,000

   Dearness allowance Rs. 6,000

   Bonus Rs. 5,000

   His contribution to RPF Rs.4,000

   His employer's contribution to the fund Rs.4,000

   Interest credited to the accumulated balance of the provident Fund at 10% Rs.3,000

   He was provided with a small car which is used both for official and private purposes.

   He incurred expenditure on books and news papers Rs.400

   He received interest on listed commercial securities (net) Rs.4,450

   He received dividend from a co-operative society (gross) Rs.470

   He paid life insurance premium of Rs.1,000 p.m. on his life insurance policy for Rs.1,50,000

   He donated to an approved institution Rs.8,000

   Compute his taxable income for the assessment year 2004-05.

11. TAX REBATE AND TAX COMPUTATION

Tax Rebate for Women below 65 years (Sec 88 C)

This rebate is applicable w.e.f assessment year 2001-02 and this rebate is allowed only to women assesses.

An assessee –

i) being a women resident in India

ii) below the age of 65 years

Tax rebate – The least of the following two amounts is allowed as tax rebate

a) Rebate is admissible at 100% of the income tax computed before claiming any rebate u/s 88, 88C and relief 89 (i).
b) Rs. 5,000

Tax rebate u/s 88C is available even from tax on long term capital gains and tax on winning from lotteries.

Tax Rebate for Senior Citizens (Sec 88 B)

Rebate under section 88B is allowed when all the following conditions are satisifed.

i) the assessee is an individual and is resident in India.

ii) he is of the age of 65 years or more at any time during the previous year.

Quantum of Rabate: Rebate is admissible at 100% of the income tax, computed before claiming rebate u/s 88 and relief u/s 89(I) or Rs.20,000 whichever is less.

Rebate U/s 88

The basic condition to be satisfied by the assessee to claim rebate u/s 88 is to make the payment during the previous year relevant to the current assessment year in the approved savings. Rebate u/s 88 is allowed to individuals and HUFs. Payments, investment, deposit in qualified savings, qualified for rebate on payment basis only. If the amount is due, not yet made, then it does not qualify for rebate.

Rebate under this section is calculated in 3 steps.

1. Gross Qualifying amount
2.Net Qualifying amount
3. Amount of deduction

Qualified Savings

The savings on which tax rebate is allowed are known as qualified savings. The government from time to time notifies the qualified savings. Premium on life insurance policy, contribution to provident fund are the examples of qualified savings. Remember on every savings tax rebate is not given. On the other hand, tax rebate is given only on approved savings. From this rule it can concluded that all qualified savings are savings but all savings are not qualified savings.

Qualified savings can be classified into two categories. They are;

1. Investment in specified securities,
2. Invest in general savigs.

Investment in special Securities

Investments in shares and debentures of infrastructure, power and telecommunication companies are known as specified securities.

Investment in General Savings

The following is the list of general savings.

1. Premium paid on life insurance policy on the life of the assessee or his/ he wife/husband/child or any member of the family (Premium amount should not exceed 20% of the policy. W.e.f. assessment year 2004-05.
2. Premium paid on deferred annuity plan on the life of the assessee/ spouse/child.
3. Amount deducted from the salary of Government employee for securing him deferred annuity or making provision for wife or children up to a maximum of 1/5 of the salary.
4. Contribution by an individual to any provident fund governed by Provident Fund Act, 1925.
5. Contribution to statutory provident fund.
6. Contribution by an employee to recognized provident fund.
7. Contribution to super annuation fund.
8. Contribution to public provident fund.
9. Amount deposited in 10-year or 15-year post- office C.T.D. Account.
10. Subscription to National Savings Scheme 1992.
11. Subscription to National Savings Certificates, VIII issue.
12. Contribution to Unit- Linked Insurance Plan (ULIP)
13. Contribution to Unit-Linked insurance policy of LIC mutual fund (Dhanaraksha plan of mutual fund).
14. Contribution to notified annunity plan of LIC (Jeecan Dhara, Jeevan Akshay of LIC)
15. Subscription to equity linked savings schemes of mutual funds not exceeding Rs. 10,000.
16. Contribution to notified pension fund by mutual funds or UTI (Retirement benefit unit scheme of UTI).

17. Subscription to home loan account scheme of National Housing bank.
18. Subscription to notified deposit scheme of a public sector company engaged in providing long-term housing finance or any authority constituted for developing housing and town planninhg.
19. Amount paid for the purchase or construction of a residential house property or for purchase of land up to Rs. 20,000
20. Tuition fee paid by the assessee towards children's education.

Rules :

a) It is applicable for two children
b) The sum should have been paid as tuition fee excluding any payment towards development fee or donation.
c) It should have been paid at the time of admission or therewafter.
d) It is paid to any school, college, university or other educational institutions.
e) It is paid for the purpose of full time education.
f) Maximum amount Rs. 12,000 per child.

Qualifying amounts for general savings is explained as follows.

1. Contribution of provident fund

Types of provident funds:

a) Statutory provident fund
b) Recognized provident fund
c) Unrecognized provident fund
d) Public provident fund

Contribution to these funds is of two types:

a) Employer's contribution
b) Employer's contribution

a) Employer's contribution to provident fund is an income to the employee, hence taxable as salary income.
b) Employee's contribution to provident fund is a saving – qualified savings is eligible for tax rebate.
c) Interest credited to the provident fund – it becomes income to the employee. Hence unexempted amount is taxable as salary.

Exempted limit and qualified amount of savings under different provident funds are given in the following table.

Provident fund

Provident Fund	Status	Employer's Contribution	Employer's	Interest
1.Statutory Provident Fund (SPF)	Applicable central /state/semi/-govt.	Fully tax free	Fully qualifies	Fully tax free
2. Recognized Provident Fund (RPF)	Public and private	Upto 12% of salary is tax free; the remaining amount is to be added to salary	Full qualifies	Upto 9.5% rate is tax free
3. Un-recognized Provident Fund (URPF)	Private	Ignore	Does not quality	Ignore
4. Public Provident Fund (PPF)	General Public	Taxable perquisite	Qualities subjects to a limit of Rs. 100 minimum Rs. 60,000 maximum	Fully tax free

Note : Refund form PF

a) Statutory provident fund and public provident fund –fully tax free.

b) URPF – Employer's contribution and interest thereon is taxable.

a. RPF: i) If the contribution is regular and continuing for more than 5 years.

ii) If resigned with 5 years – Fully tax free.

iii) If removed from the service within 5 years – Fully tax free.

Note: The interest which accrues on NSC VII issue qualified for deduction u/s 80 L and also for rebate u/s 88.

2. Life Insurance Premium

Premium paid on own policy or spouse or on children or joint policy whether paid by the employer or employee. Actual premium paid fully qualifies for rebate provided the policy is not discontinued within 2 years.

Note: Employer paid premium should be again treated as perquisite and added to the salary.

3. Payment of principal amount on housing loan

If the assessee has borrowed the money from government (Central/State) of bank (commercial/corporation) or LIC or any housing boards for construction of a house, the repayment of loan installments qualifies for rebate u/s 88 to the extent of Rs. 20,000.

(All other general savings qualify for rebate on actual basis subjects to the limits given in the income tax act.)

Steps

Step1: Gross Qualifying amount : Take the total of qualifying amounts under savings.

Step2: Net qualifying amount

a) In case of general savings : The overtime limit is least of the following two amounts.
i) Aggregate of qualifying amounts under different savings
ii) Rs. 70,000

b) In case of special savings : The overall limits is least of the ` following two amounts
i) Actual amount interested
ii) Rs. 10,000.

Note: Maximum overall limit for general and specified savings both is fixed at Rs. 1,00,000 only. If the assessee wants to claim the maximum tax rebate he/she should invest Rs. 30,000 in specified investments. Otherwise the over all limit will be restricted to Rs. 70,000.

Example

S. No	Investment on PPF & others including sun paid as tution fee for 2 children (general savings) Rs.	Investment in infrastructure and power bonds Rs.	Amount eligible for rebate Rs.
1.	70,000	20,000	90,000
2.	7,00,000	30,000	1,00,000
3.	80,000	Nil	70,000
4.	Nil	1,10,000	1,00,000
5.	70,000	10,000	80,000
6.	80,000	5,000	75,000
7.	75,000	15,000	85,000
8.	60,000	40,000	1,00,000

Step 3- Calculating tax rebate

Quantum of Rebate: Rebate of income tax under section 88 after applying the above maximum aggregate limit has been restricted depending upon the gross total income of the assessee as under.

a) When the income from salary of the individual before claiming deduction under 16 does not exceed Rs. 1,00,000 and his income chargeable under the head salaries is not less 90% of the gross total income of the individual.

Tax rebate: 30% of eligible savings/ investments

b) Where the gross total income of individual or HUF (before claiming deduction under chapter VIA) does not exceed Rs. 1,50,000

Tax rebate: 20% of eligible savings/ investments subjects to maximum rebate of

General : 70,000 x 20% = Rs, 14,000

Overall : 70,000 + 30,000 x 20% = 20,000 as the case may be.

c) Where the gross total income (before claiming deduction under chapter VIA exceeds Rs. 1,50,000 but does not exceed Rs. 5,00,000.

Tax rebate : 15% of eligible savings / investments subject to maximum rebate of

General :70,000 x 15% = 10,500

Overall : 70,000 + 30,000 x 15% = Rs. 15,000 as the case may be.

d) Where such gross total income of individual or HUF exceeds Rs. 5,00,000

Tax rebate : Nil

Tax computation of casual income was already explained in Chapter-4.

Types of capital gains

1. Long -term capital gains [2(29B)]
2. Short-term capital gains [2(42B)]

Long –term capital gains

'Long –term gains' means capital gains arising from the transfer of a long- term capital asset.

Short – term capital gains

'Short –term capital gains' means capital gains arising from the transfer of short – term capital asset.

U/S 45 (1) any profit or gains arising from the transfer of capital asset effected in the previous year shall 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 said definition can be split into two important parts.

a) income arising from the transfer of capital asset
b) transfer effected in the previous year and it becomes imperative to study both parts in detail.

Illustration

Ram is a Professor in a Mumbai College getting salary @ Rs. 15,000 p.m. plus 22% on account of Dearness Allowance. He contributes 12% of his salary to Recognized Provident Fund and employer contributes the same amount. He is also hostel warden and has been provident with rent – free unfurnished accommodation whose rental value is Rs. 12,000 p.a. He owns a house, which is let out at Rs. 800 p.m. and he pays municipal taxes amounting to Rs. 1,600 p.a.

During the previous year, he received the following incomes:

a. 10% dividend on shares of Rs. 12,000
b. 15% dividend on Rs. 20,000
c. 12% interest on debentures of Rs. 60,000
d. Rs. 4,600 being one – third share of profits in an AOP
e. Rs. 2,400 dividend from a company
f. Rs. 4,000 as interest on bank deposits.

He has insurred his for Rs. 1,25,000 and paid Rs. 13,250 as annual premium. Ascertain his Total Income.

Solution

Computers of Total Income of Ram for the assessment year 2004 – 05

	Rs.	Rs.
Income from Salaries		
Salary	1,80,000	
D.A. @ 22%	39,600	
Value of rent free house:		
Salary of the employee = 1,80,000		
10% of salary	18,000	
Gross Salary	2,37,600	
Less: Standard deduction	25,000	
Income from Salaries		2,12,600
House Property		
Annual rental value	9,600	
Less: Municipal taxes	1,600	
Net Annual value	8,000	
Standard deduction @ 30% of NAV	2,400	
Income form House Property		5,600
Profits & Gains		
1/3rd share from AOP – Exempted		Nil
Other Sources		
Dividend on shares 10%	1,200	
Dividend on units	3,000	
Dividend	Nil	
60,000 12% Debentures	7,200	
Interest on Bank Deposits	4,000	
Income from Other Sources		15,400
Gross Total Income		2,33, 600
Less: Deduction u/s 80L		
Bank Interest + Dividend		9,600
Total Income		2,24,000
Computation of Tax Liablity		
	Rs.	Rs.
Tax on Rs. 1,50,000 of total Income		19,000
On balance Rs. 73,000		21,900
		40,900
Less: Rebate of tax u/s 88		
QA: Own contibution to PF	21,600	
Life Insurance premium	13,250	
	34,850	
Rebate @ 15% of QA		5,228
Balance Tax / Tax Liability		35,672

SUMMARY

Tax Rebate for Women below 65 years (Sec 88 C)

This rebate is applicable w.e.f assessment year 2001-02 and this rebate is allowed only to women assesses.

Tax Rebate for Senior Citizens (Sec 88 B)

Rebate under section 88B is allowed for senior citizens.

Rebate U/s 88

The basic condition to be satisfied by the assessee to claim rebate u/s 88 is to make the payment during the previous year relevant to the current assessment year in the approved savings. Rebate u/s 88 is allowed to individuals and HUFs. Payments, investment, deposit in qualified savings, qualified for rebate on payment basis only. If the amount is due, not yet made, then it does not qualify for rebate.

Long –term capital gain

'Long –term gain' means capital gains arising from the transfer of a long- term capital asset.

QUESTIONS

1. How do you compute income tax liability of an individual assessee ?

2. Mohan submits the following particulars relating to his income for the previous year 20003-04. Compute total income and the tax liability of Mohan for the assessment year 2004-05.

   a. Salary from a public sector company in Delhi after deduction of income tax and provident fund contribution Rs. 84,000
   b. Income tax deducted at source. Rs. 6,000
   c. Contribution to recognized provident fund Rs. 18,000
   d. Employer's contribution to provident fund Rs. 12,000
   e. House rent allowance at 12% of salary (actiual rent pid by X- Rs. 3,500 p.m.)
   a. Leave travel allowance from employer of which 75% was spent on travel to hometown Rs. 12,000
   b. Rental income from house Rs. 10,500.
   c. Municipal value of house Rs, 48,000
   d. Standard rent determinable Rs,24,000
   e. Municipal taxes Rs. 6,000
   f. Interest on aloan of Rs. 1,00,000 at the rate of 15% p.a. in respect of purchase of house Rs. 15,000
   g. Deposit in Cumulative Time Deposit of Post Office Rs. 15,000
   h. Purchase of National Savings Certificates VIII Issue Rs. 25,000
   i. Purchase of units of CANBANK mutual fund Rs. 5,000
   j. Payment of mediclaim premium Rs. 1,500
   k. Donation to an approved temple Rs. 11,000

(**Answer:** Total Income Rs . 1,43,000; Rebate u/s 88: Rs. 9,000 ; Net tax Rs. 8,600)

GLOSSARY

Assessment Year	=	Tax paying year
Assessee	=	Tax paying person
Association	=	Union
Accrue	=	Arise
Ambassador	=	Representative of a nation
Assessing Officer	=	Any officer who is empowered to collect the tax and perform such proceedings under the Income Tax Act
Assessment	=	Determination of the total income of an assessee
Casual	=	Unexpected
Consular	=	Representative of foreign power
Deduct	=	Deciding
Disablement	=	Loss of physical power
Depreciation	=	Decrease in the value of asset
Deemed	=	Considered
Encashment	=	Convert into cash
Empowered	=	Give power to
Exception	=	Deviation from the rule
Gains	=	Profits
Gratuity	=	Gift for service
H.U.F.	=	Hindu Undivided Family
Income Tax	=	Tax on income
Incidence	=	Happening
Jurisdiction	=	Extent

Karta	=	The head of a H.U.F.
Liability	=	An obligation
Levy	=	Impose tax
Misappropriation	=	Use wrongly
Nationalisation	=	Bring under the control of the Govt.
Offences	=	Crimes
Previous year	=	The year proceeding the assessment year
Permanent	=	Forever
Pension	=	Monthly payment after retirement
Perquisites	=	Additional benefits
Retrospective	=	From back date
Refunds	=	Pay back
Surrender	=	Act of giving up
Set off	=	Adjust
Securities	=	Bonds
Taxable	=	Subject to tax
Vital	=	Important

<u>**REFERENCE BOOKS**</u>

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